

JANUARY 1956

Mortgage Banker



in this issue -----

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MBA 1956 Calendar

January 24, 25 and 26, 1956, Senior Executives Conference, New York

February 22, Board of Governors Meeting, Conrad Hilton Hotel, Chicago

February 23 and 24, Midwestern Mortgage Conference, Conrad Hilton Hotel, Chicago

March 12, Mortgage Servicing Clinic, La Salle Hotel, Chicago

March 14, Mortgage Servicing Clinic, Hotel Statler, Washington, D. C.

March 16, Mortgage Servicing Clinic, Andrew Jackson Hotel, Nashville

April 5-6, Southeastern Mortgage Clinic, Hotel John Marshall, Richmond

April 7, Board of Governors Meeting, Dinkler-Plaza Hotel, Atlanta

April 9-10, Southern Mortgage Conference, Dinkler-Plaza Hotel, Atlanta

April 30-May 1, Eastern Mortgage Conference, Commodore Hotel, New York

May 10-11, Southwestern Mortgage Clinic, Hilton Hotel, Albuquerque

May 14-15, Western Mortgage Conference, Mark Hopkins Hotel, San Francisco

May 18-19, Northwestern Mortgage Clinic, Olympic Hotel, Seattle

June 24-July 7, School of Mortgage Banking, Courses I, II and III, Northwestern University, Chicago

July 29-August 11, School of Mortgage Banking, Courses I and II, Stanford University, Stanford, California

October 8-11, 43rd Annual Convention, Conrad Hilton Hotel, Chicago

The Mortgage Banker

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FINE WOOD HOMES BY UNITED



Report of Testing of Advertised Products

PACKAGED HOUSING is on the agenda this month. Parents' Magazine's consulting engineers have been investigating United States Steel Homes. You'll find many of these prefabricated houses in almost every state of the union. They have withstood the wear and tear of varying climatic and weathering conditions. Their excellent reputation in the factory-built homes field is due in large part to high standards of quality control at the manufacturing plant in New Albany, Indiana, where structural units and component parts are manufactured and assembled.

OUR ENGINEER CONSULTANT, Dr. A. E. Surosky, of The United States Testing Company, Inc., field-inspected a group of houses in process of construction. The popular ranch style, "Coronado," a three-bedroom house, was at that stage of construction where Dr. Surosky could examine and compare materials and workmanship with specifications and construction details he had witnessed during manufacture. While the builders went about their work Mr. Surosky checked among other things for trueness of panel construction, size and type of bolts used at strategic points, character of insulating material and neatness of trim. Like all conventional as well as prefabricated, United States Steel Homes, Inc., must meet certain Federal requirements for structural strength. For example, ceiling and wall panels, basic units in a prefabricated house, must be able to withstand certain stress loads as prescribed by Department of Commerce specifications. This test work was conducted for United States Steel Homes by the Institute of Industrial Research at the University of Louisville. For example, wall panels made of wooden frames to which plywood is glued, showed no signs of damage to any part of the panel when subjected to an impact load 50 percent

greater than is actually required by test specifications. Roof panels, doors and truss units, the latter used in homes with a pitch to the roof, also withstood similar impact tests calculated to meet sound building construction requirements.

PREFABS AND WIND VELOCITY. United States Steel Homes, Inc. have had their mathematicians translate load resistance of a panel into wind load. By way of dramatizing the strength of the panel construction, the math boys figure that a load of 4615 lbs. on such a panel is equivalent to a gale force of approximately 238 miles per hour. Of course other factors influence resistance to winds of hurricane velocity but, in general, prefabs are known to have ridden out Atlantic coast hurricanes when conventional houses were badly damaged.

PLANT INSPECTION. Examination of independent test data supplemented Dr. Surosky's inspection of the manufacturing operation. His report to Parents' Magazine stresses the fine quality of raw materials such as lumber, plywood, hardware, and the equally important close inspection exercised along the assembly line. United States Steel Homes, Inc., buys many materials in carload lots. Quantity buying can mean price savings to pass along to the dealer-builder and thence to the consumer. High inventories maintained by the factory mean less deterioration and probable losses at the building site. For the prefabricated house is delivered in one package and to order only. The consumer benefits from the know-how of skilled architects and construction engineers who have calculated to the fraction of a pound of nails or board foot measurements what is needed to construct a "Coronado" or any one of the many attractive United States Steel houses.



Products eligible for Parents' Magazine's Commendation Seal are awarded the Seal only after Parents' Magazine's technical staff and/or medical consultants have studied them and the claims made for them. The United States Testing Company, Inc. is employed on an annual retainer to do whatever tests are required.

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Why Parents' Magazine likes them

This editorial feature from the July issue of *Parents' Magazine* explains why United States Steel Homes are good buys . . . why they are assets to any community. Read it and learn why.

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LOTS OF ACCEPTANCE — Thousands of eager home buyers flocked to the Bride's Houses featured by United States Steel Homes Dealers last spring. Two thousand people bought homes—right on the spot. More sales success marked the Personalized Coronado promotion last fall. Continued national advertising and local promotion is building the reputation and acceptance of United States Steel Homes Dealers and the homes they build. These homes are good; they are attractive; they are popular. The quality construction and intensive advertising that builds sales now will keep resale value high.

LOTS OF HELP FOR DEALERS — A United States Steel Homes Dealer is on a much sounder footing than the

average builder, because he has all the resources of United States Steel behind him. Our help and advice on land planning, financing, selling, building eases him over the rough spots and assures sound planning.

Prefabrication, by its very nature, helps him to greater success. It enables him to build faster at lower cost. It enables him to offer extra value. And it assures you of uniform quality, house after house.

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A large percentage of the mortgages made today are made by the mortgage banker. A larger percentage of the mortgages held in the portfolio of the principal for whom the mortgages were made are FHA or GI *guaranteed* mortgages.

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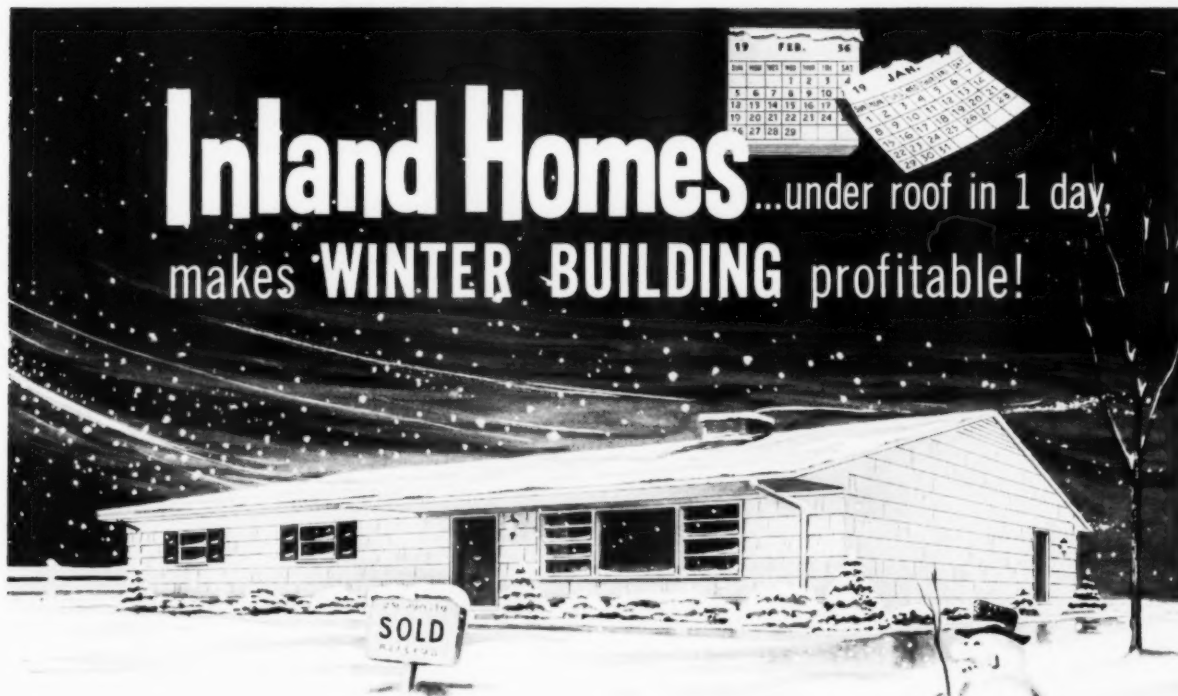
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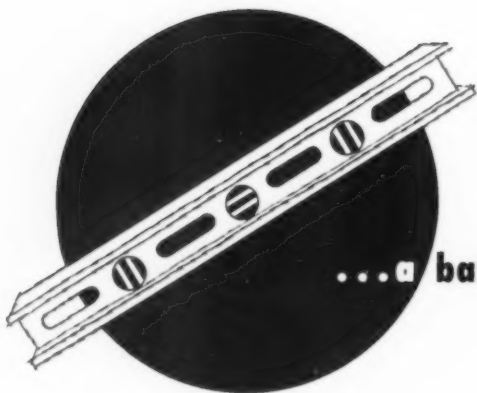
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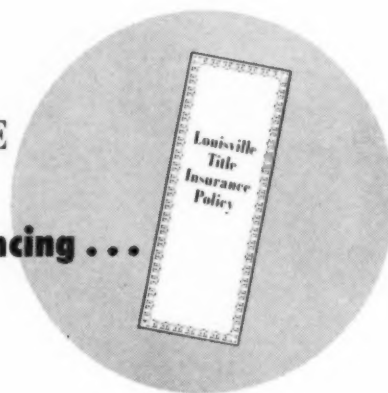
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Most Prosperous Decade in History

It's been just that—the biggest decade this nation or any other ever knew. The American economy is now some four-fifths bigger than it was at the end of World War II in gross national product. More than \$700 billion has been spent by the people and by business since the beginning of 1946 to expand their tangible wealth in the form of producers' and consumers' durable goods.

For the 1946-55 period, the figures break down this way:

» A total of more than \$340 billion in business investment, predominantly in new plant and equipment, commercial construction and inventories.

» Close to \$260 billion in consumer durable goods, of which automobiles represent nearly one-third; and

» More than \$100 billion in residential non-farm housing.

This accomplishment in such a comparatively short space of time is without parallel in the history of this or any other nation.

Total long-term savings of individuals are now in the neighborhood of \$230 billion, some \$90 billion more

than they were a decade ago. Life insurance protection in force is currently well over \$350 billion, or more than double the total outstanding at the end of 1945.

Assets of private pension funds, insured and non-insured combined, which now cover about one out of every four workers excluding those in agriculture and on the public payroll, are rapidly approaching the \$25-billion mark. They added up to \$21 billion at the end of 1954, and are growing at the rate of about \$3 billion a year.

But at the same time people have gone heavily into debt to buy their homes, cars and other tangible possessions, and business borrowings have increased greatly as well. Net debt in the private sector of the economy—corporate, individual and noncorporate combined—more than doubled in the 1946-54 period to exceed \$340 billion at the end of 1954. Personal debt has shown the greatest relative increase in the period. It is the rapidity of the rise more than the over-all size of the debt that has aroused some concern, and explains the recent credit restraints imposed by govern-

mental authorities to help prevent the boom from getting out of hand.

More than 10 million new non-farm dwelling units have been built in the period since the end of World War II. This has been accompanied by a new peak in home ownership, with an estimated 55 per cent of all homes in the country now owner-occupied.

These and other investment-type expenditures by the people and by business, combined with the needs of government, have brought a record demand for funds on the capital market. The capital market supplied a total of \$200 billion in new money to business and industry, homeowners, and government (Federal, State and local combined) in the 1946-54 period.

This figure accounts only for the net increase in outstanding loans and investments which passed through the capital market in the period, and does not include retained earnings invested by business firms and other direct expenditures for construction, real estate, and inventory. The people's savings supplied nearly two-thirds of all the net new capital funds made available in the 1946-54 period, evidence of the dynamic role of personal thrift in economic progress.

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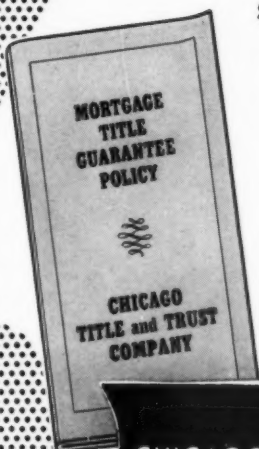
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MORTGAGE FINANCING IN THE COUNTRY'S CREDIT STRUCTURE

A Statement by

WILLIAM McC. MARTIN, JR.

Chairman, Board of Governors of the Federal Reserve System

It wasn't so true a generation ago but one of the facets of the mortgage business today that anyone in it must understand fully is the broad field of credit—all the influences which establish credit terms and climate, how federal fiscal policy works and, more important, how mortgage credit fits into the overall picture. Chairman Martin, in his appearance before the Subcommittee on Housing of the Senate Banking and Currency Committee, made a statement which is a good explanation of what is involved as far as our business is concerned. This is his text.

CONGRESS has placed on the Federal Reserve System responsibility for formulating and carrying out national credit and monetary policies. The System's objective is to contribute to sustainable economic growth and to maintenance of a stable value for the dollar. This responsibility for credit and monetary conditions relates to the over-all credit situation, not to markets for particular goods and services or to the activities of particular producer or consumer groups.* The System's actions influence most directly the lending and investing activities of commercial banks, which supply the credit used by individuals or business. These operations of the commercial banks, in turn, influence other financial institutions and markets.

The general economic developments with which the System is primarily concerned are the result of combined activities of the many markets that make up the economy. The System must keep itself informed constantly about these particular markets in order to make judgments and to determine appropriate credit and monetary policies.

Response to the Subcommittee's inquiry about the influence of credit and monetary policy on mortgage and housing markets must be considered

against this background. As these are specific markets, the influence of credit and monetary policies upon them is indirect.

The amount of housing that may be built, sold and financed within any period depends upon a number of considerations. Demand for housing depends on growth and shifts in families and other occupants, upon price factors, and upon ability of individual buyers to finance their purchases. It also depends upon the physical availability of resources for construction

of new homes—land, building materials, and labor. This places definite limits on the amount of housing that can be added to the supply within any short period of time.

The capacity of the economy to finance home purchases must also be considered. The availability of funds for investment in mortgages depends on the flow of savings, on alternative opportunities for investing funds, and on credit and capital market conditions generally.

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chases are strongly influenced by the availability and terms of credit. The nature of this influence is not easy to trace, for many other factors are always at work. It is clear, however, that because of the complexity of these markets, the impact of credit and monetary policy on their different sectors and on participants therein varies considerably.

Because mortgage markets are local in important respects, variations usually develop among geographic areas, reflecting different market structures as well as differences in regional economic development. To a considerable extent the development of Federally underwritten mortgages has served to reduce regional differences in the supply of savings relative to local investment demands. The relative attractiveness of Federally underwritten mortgages and conventional mortgages may change from time to time, partly because interest rates on the latter are free to vary more widely than are rates on the former.

The effects of changes in credit and monetary policy normally take some time to permeate a market as complex and variable as the mortgage market. They may be particularly slow to influence construction, for instance, if the amount of financing commitments by lending institutions is large. The precise timing of events cannot be foreseen in view of the many variables involved and the changing circumstances of each period.

For example, from mid-1952 to mid-1953 large over-all demands for credit pressed upon limited, though growing, credit availability and resulted in some strains on financial markets. Expansion of real estate mortgage debt was restrained at the start of this period by the selective regulation of real estate construction credit. Regulation X, governing the extension of conventional credit on new houses and other new structures, was suspended in September 1952, but some restrictive conditions on Federally underwritten mortgages continued until April 1953.

Federally underwritten mortgages having relatively low maximum interest rates became less attractive to investors in a market of generally rising yields, and were salable only at discounts from par. GI loans on new houses, in particular, declined mark-

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edly during the year ending June 1953 and were a much smaller proportion of total mortgage lending than in comparable earlier periods. Conventional mortgage lending meanwhile increased substantially, although such loans were generally available to borrowers only at higher interest rates and on more restrictive terms than had been the case prior to selective credit regulation and general credit restraint.

Interest rates on Federally underwritten mortgages were raised in May 1953. Shortly afterwards, the slackening of other credit demands, the easing in credit and monetary policy, and the resulting decline in yields on non-mortgage investments improved the competitive position of mortgages generally in financial markets. Moreover, the flow of savings to financial institutions was increasing rapidly while issues of corporate securities available to investors were reduced.

The Change Began in 1953

The changed demand and supply situation in financial markets began to be reflected significantly in mortgage markets late in 1953. By that time, with slackening in other demands for credit and a continuing decline in yields on competitive investments, funds for mortgages with Federal underwriting became much more readily available, with both FHA and VA loans selling in secondary markets at prices close to par, and interest rates on conventional loans reduced by $\frac{1}{4}$ to $\frac{1}{2}$ per cent. Investors began actively to seek mortgages on terms which they would not have granted six months earlier. Commitments by lenders to take mortgages, especially those guaranteed by VA, were made in increasing volume toward the end of 1953 and rose sharply in 1954, and many lenders who earlier did not engage in such activity began to do so.

The rise in mortgage credit on newly completed and existing properties did not occur until the second half of 1954. In that period total mortgage lending was one-fourth larger than in the preceding six months, reflecting gains in most types of loans for purchase of both new and existing houses. GI loans were increasingly available to borrowers with no down payment and maturi-

ties of 30 years, and other types of mortgage loans were also readily available on favorable terms.

Mortgage lending on residential properties expanded sharply in the first half of 1955 to an all-time high of almost \$14 billion. The volume of GI loans made on new houses rose markedly to over \$2 billion, the largest total by far for any half year. In the same period there was a sharp rise in FHA-insured loans on existing houses to over \$900 million, reflecting chiefly a liberalization of terms made possible by the Housing Act of 1954.

New Records in 1955

For the full year ending June 30, 1955, new records for nearly all types of mortgage lending were established. The ready acceptance by investors of VA-guaranteed loans on terms favorable to borrowers and the accumulation of a large backlog of commitments by lending institutions, to take mortgages in the future, stand out as major influences on the mortgage market during this period. Increase in the volume of VA loans amounted to over two-thirds of the increase in lending on new houses and over two-fifths of the increase in lending on existing houses. Meanwhile, FHA-insured loans made on new houses during these 12 months showed little change from the two preceding 12-month periods.

The influence of credit conditions on home building and purchase is even more difficult to trace than that on mortgage markets, particularly as far as the timing of changes is concerned. For example, there was little decline in residential construction activity as a result of the credit stringency in the spring of 1953. Subsequently, there was considerable lag in the adjustment of residential market activity to the change toward easier credit availability which began around mid-1953. The number of housing units started through the first half of 1954 was little different from comparable periods in preceding years. Statistical measures of pre-building activity did not begin to move upward until early 1954, but thereafter rose rapidly. By August, requests by builders to VA for appraisal of proposed houses were more than double the largest monthly total in the three

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preceding years. Applications to FHA for mortgage insurance on new houses also reached considerably higher levels in the summer and autumn of 1954 than in previous comparable periods.

How Building Expanded

Reflecting the upsurge in pre-building activity, new private housing starts beginning in June 1954 increased contra-seasonally through the end of the year, with monthly totals in the last quarter the largest for any comparable month on record. The substantially larger volume of units started in the second half of 1954 compared with the like period of 1953 reflected chiefly a more than doubling in units started under VA guarantee. Units started under FHA financing arrangements also increased slightly, while conventionally financed starts declined.

Sales of old as well as new houses accelerated in the second half of 1954 and continued strong through the middle of 1955. In the 12 months

ending June 1955, substantially more houses were sold than during preceding comparable periods. Reflecting the impact of easing terms in the GI loan market during 1954, the increase in units sold with VA-guaranteed mortgages in the year ending June 1955 amounted to almost two-thirds of the increase in new house sales and nearly two-fifths of the increase in existing house sales.

Last summer and autumn eco-

nomie activity in most lines had been at new high levels. The gross national product in the third quarter was a record \$392 billion (seasonally adjusted annual rate) and a further large increase is indicated for the current quarter. In October, industrial production continued at the new high established in September and nonagricultural employment was a record for any October.

The most striking economic devel-

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opments over the past year have been the marked expansion in consumer buying, especially of durable goods, renewed rise in business outlays for fixed capital, and the relatively moderate nature of inventory accumulation. Since output in many areas is now close to capacity, further increases in production will necessarily be at a slower pace and growth in consumption and investment demands will need to be correspondingly moderated.

Reflecting the pressures of expanding demands upon limited supplies, wholesale prices of industrial commodities have been rising considerably since mid-year, with the increases more recently extending to intermediate products and finished goods. Consumer prices, which have been relatively stable for two years, have recently shown signs of edging up.

The situation is not greatly different in construction and real estate markets, except that these markets have been extraordinarily strong for a longer period. Since the recovery in the general economy began more than

a year ago, activities revolving about construction and real estate, which continued high throughout the 1953-54 recession, have expanded sharply further and are now at record levels. The evidence in recent months suggests increasingly that construction and real estate activities—even more markedly than most manufacturing activities—are close to capacity. In these areas, as in the economy as a whole, a major current problem is to prevent development of inflationary forces, which could lead to serious maladjustments and declines from the gratifying levels of activity experienced in recent years.

Price Increases Back

The recent volume of construction and high levels of economic activity generally have resulted in large and widespread price increases for building materials. After about two years of comparatively easy material supplies and efficient operations, materials shortages and delays in the progress of work have reappeared. Likewise, financing—in competition

with many other expanded demands in a capital market characterized by large, though limited, supply—has become more difficult and more expensive for many types of undertakings.

Some observers in recent weeks have attributed these developments and the moderately reduced level of starts solely to a more restrictive monetary policy. This is by no means an adequate explanation. For example, although housing starts for some months have been below the very high levels reached last spring, the number of houses under construction this summer was probably larger than ever before. If construction delays have been as serious as some trade reports suggest, this number may still be rising. The number of new houses completed and occupied in the first six months of 1955 was considerably larger than in any other first half year. Completions in the second half will undoubtedly rise further to exceed the all-time record second half of 1950.

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Relatively Few Veterans Use Home Loan Rights

Only 17% Have Accepted Opportunity in Area; Figure is 27% for 75 Centers

Only about 17% of the eligible veterans in the take-out area have taken their rights.

area, only 17,005 home loans guaranteed by the veterans' administration had been closed during the 10 year period which ended Jan. 1, according to the report. About 2,800 of these were closed during 1954, a new jump over the total for the

Half Veteran Population



It was 132 years before the SECOND white man saw TENNESSEE

Hernando de Soto was first, reaching the Mississippi River in 1541, at or near the present site of Memphis.

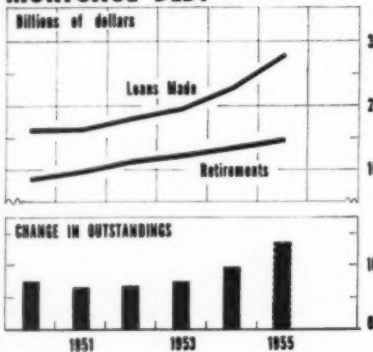
But the *second* white man to visit Tennessee came 132 years later — that famous French missionary-explorer, Father Marquette, who voyaged down the River by canoe in 1673.

Today, with population in the millions, *agriculture and commerce*, highlighted on Tennessee's Great Seal, epitomize the productivity that throbs throughout its prosperous 42,000 square miles.

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MORTGAGE DEBT



Mortgage lending has increased much more rapidly than debt repayment in recent years, so that the outstanding debt has continued to rise. Last year the increase was probably about \$13

billion, compared with \$9.7 billion in 1954 and \$7.6 billion in 1953. The total amount of home mortgage debt outstanding at mid-1955 was \$82 billion and was probably about \$89 billion at year-end. This is double the amount outstanding as recently as the end of 1950 and almost 5 times as high as at the end of the war. In the past year federally-underwritten mortgage debt has risen somewhat more rapidly than conventional, and currently well over two-fifths of total home mortgage debt is guaranteed or insured by the federal government.

It is the rapidity of the increase of mortgage debt that has concerned many economists during the past two years.

These completions have required an exceptionally heavy volume of financing. In addition, sales of an unprecedented number of old houses have also been financed. Accordingly mortgage lending during last year was at record levels, more than one-fourth higher than in the comparable period of 1954. Demands for financing are still rising. Whatever effects the present credit situation may be having on housing markets, it has not prevented

an extraordinarily large volume of mortgage underwriting. It is the large demands for credit throughout the economy, rather than a curtailment of funds for investment in housing, that has caused a tightening in the money market.

Mortgage repayments have also been rising, but at a slower rate. As a result, the amount of mortgage debt outstanding has been growing rapidly. Mortgage debt outstanding on

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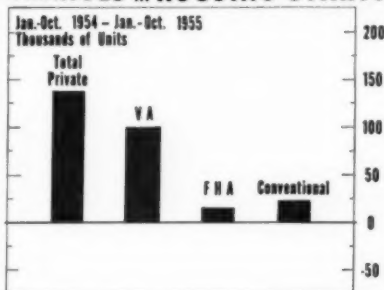
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CHANGES IN HOUSING STARTS



Comparing the first 10 months of 1955 with the like period of 1954, most of the increase in housing starts has been in units started under VA guarantee. The number of VA starts was more than two-fifths larger in the first 10 months of 1955 than

last, and amounted to 30 per cent of total private starts, larger than in any preceding comparable period. Many of these units have been available to borrowers with no downpayment and 30 years to pay the mortgage.

VA expects 1956 to run about the same rate as 1955, with about 650,000 applications as against a record 630,000 in 1950 and about 528,000 in 1954. VA estimates that this year 400,000 applications will be for new construction and the remaining 250,000 for existing construction.

VA spokesmen base their predictions partly on an expectation of an easier money market.

small properties last year can be expected to increase by about \$13 billion compared with \$9.6 billion in 1954.

Last year's increase in all non-farm mortgage debt will be close to \$16 billion, and of this over \$11 billion will be acquired by three major groups of lenders—savings and loan associations, mutual savings banks, and life insurance companies. This is a very large proportion of the total increase this year in the capital and liabilities due from these institutions

to the public. In other recent years the increase in their capital and liabilities to the public exceeded the increase in their mortgage holdings by a wider margin.

To obtain the funds needed to keep up the recent high and rising level of mortgage lending and to meet other financing demands which have also been large, these institutions have been borrowing heavily last

(Continued on page 35)

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Most Dynamic Fact of the Future: Our FAST-GROWING POPULATION

It's probably the most significant fact in any long-term appraisal of the future—our rapid growth in population and all that it means for our economic welfare. General population trends can be predicted but the forecasters can be wrong—as many of them have been in failing to properly anticipate the growth we are witnessing. Here's a scientific observation of U. S. population, based upon studies by the Kansas City Federal Reserve Bank, as to just what has been happening, why and what is likely ahead.

THE population of the U. S. numbered more than 165 million in July of last year. This estimate exceeded the 1950 Census count by about 14 million, or more than 9 per cent, and represented a continuation of the broad upsurge since 1940. The striking change in the rate of population growth during recent years is primarily the result of a sustained increase in births. During the war, the birth rate rose materially, registered a further sharp rise after demobilization, and has held at high levels during subsequent years.

We have witnessed not only a marked increase in population size during the last decade and a half but also significant changes in other demographic factors. The most pronounced increases occurred in the number of young children under 5 and 10 years of age and in the number of persons 65 years and over. The proportion of married adults increased substantially. Household formation, following several years at

high levels, is now increasing more slowly, although total population continues its rapid expansion. Finally, important population shifts occurred during the war and postwar years—primarily the movements from the city to the suburbs and to the far west.

From the viewpoint of demand, all of this adds up to two significant points. *First*, the potential civilian demand for goods and services has never before been equaled. *Second*, the pattern of consumer demand is being modified by the requirements of our changing population.

The implications of these facts for private business and government are momentous. Increasingly, those in business and government circles are showing greater awareness of our changed population outlook. This is fortunate. Population is a major long-run factor which should be considered in economic policy decisions. The success of private business plans for capital expansion, product diversifi-

cation, and marketing programs may be enhanced by foreseeing population developments. Similarly, government—at all levels—requires long-run projections in order to formulate adequate policies relative to taxes, public works, community development, and other activities.

The primary purpose here is to summarize population changes since about 1940; to indicate some developments that may emerge in future years; and to suggest implications for long-run demand, without attempting to be exhaustive. Although population factors enter into the supply side of our economic equation via the labor force, consideration of potential output is not in the focus of the present discussion.

Prior to World War II, economic thinking was conditioned strongly by a declining birth rate and the prospect of a static population. The longstanding decline in the birth rate was accelerated in the 1920's and early 1930's, and the total number of births

dropped. Net immigration fell to insignificant levels. The average annual rate of population increase during the 1930's was about 0.7 per cent.

This outlook, together with the heritage of the depression and the passing of the geographical frontier, brought forth the concept of economic maturity. Today, that thinking appears to have been no more than a passing phase because the trend of population growth has undergone a dramatic upheaval.

Entering the decade of the 1940's, total population was slightly more than 132 million. The birth rate was moderately higher than in the mid-1930's, and population growth was on the upgrade. The expansion gained momentum as the birth rate rose during the early years of the war and jumped sharply in 1947. In succeeding years, with the birth rate holding only slightly below the 1947 level, population growth averaged 1.7 per cent per year. This is almost two and a half times the 1930-39 average.

Translating these rates into numbers reveals the absolute magnitude of current population growth. Since 1945, the average annual number of births has been nearly 3.8 million. After taking into account deaths and net immigration, total population increased an average of well over 2.6 million a year between mid-1946 and mid-1955. This is the numerical equivalent of adding the 1950 population of Colorado and Nebraska each year.

Looking ahead, it is estimated that the total population of the United States in 1965 will range from 186 to

193 million. The various projections are based on assumed levels of fertility, mortality, and net immigration, together with the assumption there will be no major wars, major economic depressions, epidemics, or natural catastrophes.

It should be noted that in releasing these projections, the Bureau of the Census considered all to be reasonably possible. In addition, it was recognized that estimates falling outside the upper and lower limits of the above projections may be reasonable possibilities.

For purposes of illustration, if 1950-53 fertility levels remain constant to 1965, average additions to population during the next decade would run about 2.5 million a year. This would suggest slightly smaller annual increments than have occurred since 1946; nevertheless, they would be quite large compared to the past.

Forecast of the Thirties

In the early and mid-1930's, business and government made plans for the market and investment requirements of a population then growing at the annual rate of slightly more than 800,000 and expected to increase by no more than some 900,000 a year during the following decade.

Now the situation is very much different. Since the end of the war, total population has increased at roughly three times those figures. Moreover, there is reason to believe that the annual increment during the next decade will continue near the level of the years recently past.

Our current population outlook

holds important implications for future levels of income and employment. Although population growth alone does not ensure high level economic activity, the stimulus of such demands in this country has been a favorable influence on activity in the past. Income and employment are stimulated not only by the consumption requirements of a rapidly growing population but also by the more favorable outlook for investment. The British economist, J. M. Keynes, expressed it in this way:

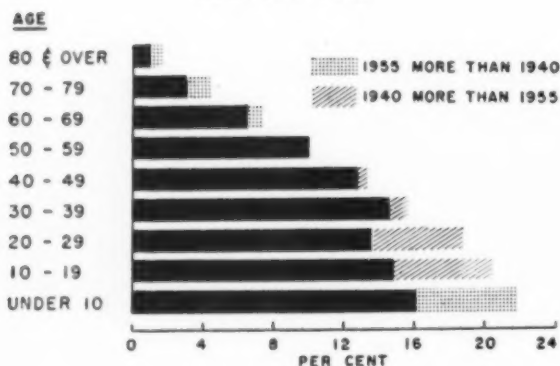
"... an era of increasing population tends to promote optimism, since demand will in general tend to exceed, rather than fall short of, what was hoped for. Moreover a mistake, resulting in a particular type of capital being in temporary over-supply, is in such conditions rapidly corrected."

An abnormally high marriage rate was the principal factor leading to higher birth rates immediately after the war. The marriage rate was higher during the early war years than during the previous prewar years and jumped to a peak in 1946. In that year, the number of marriages reached 2.3 million. A larger number of persons reaching marriage age, a lowering of the average age at marriage, and the increased proportion of the adult population who married contributed to the growth in marriages.

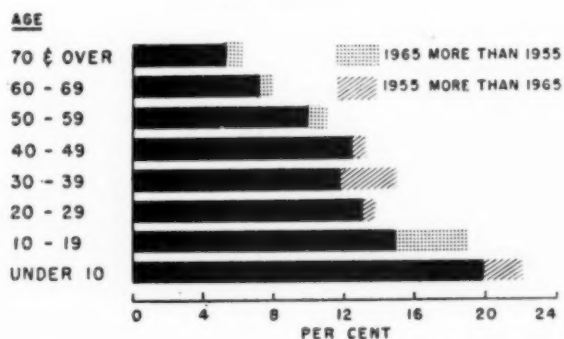
Since 1946, the marriage rate has declined rather steadily. The total number of marriages in 1954 was estimated at less than 1.5 million with a rate of 9.2 marriages per 1,000 pop-

DISTRIBUTION OF UNITED STATES POPULATION BY AGE

1940 and 1955



1955 and 1965*



ulation. This was the first year since 1944 that marriages fell short of the 1.5 million level and the rate was the lowest since 1933.

The decrease in marriages since 1946 is related to several factors. As a result of the low birth rates in the 1930's, the number of young people of marriageable age has declined. During the first half of the current decade, the number of females reaching the median age of first marriage (20 years) was the lowest for any 5-year period since the 1920's. Only 5.3 million females were between 15 and 19 years old in 1950 compared with over 6 million in 1940. Looking ahead, the number in marriageable-age classes will increase only slightly during the last half of the decade (about 5.5 million were in the 15-19 age class in July 1955) and rise substantially after 1960.

A second factor in the decline is the decrease in the single adult population. In 1954, two thirds of the females over 14 years of age were married compared with 60 per cent in 1940. During the same time, the number of single females (over 14 years) declined by nearly 3 million. In part, the increased proportion of married females arises from changes in the age distribution of the population, the decline in the marriage age since 1940, and favorable economic conditions. In addition, marriage apparently has become a more desirable goal because the decline in the number of single persons since 1940 makes a distinct break in the long-term upward trend.

Fewer marriages have resulted in no corresponding drop in births as yet. More than 4 million babies were born in 1954, making it the fourth successive record-breaking year. A large share of the births in recent years is attributable to the growing number of children per family. The significance of this influence is disclosed by statistics relating to birth rates by order of birth. Second, third, and fourth births have increased noticeably since prewar years. The rate of second births (per 1,000 native white adult females), for example, increased 65 per cent from 1940 to 1952 and came near the rate for first births. The third order rate nearly doubled during the same period. In 1953 and 1954, these higher order

births probably increased still more because it is not expected that the number of first births will show an increase.

Nevertheless, it is reasonable to expect a dip in births in the current decade. The Bureau of Census projections, which assume a continuation of 1950-53 fertility rates for given age groups of females to 1965, show a decline in the general birth rate between 1955 and 1965. Even the projection of birth rates based on the somewhat higher 1954-55 fertility rates dips slightly in the period 1960 to 1965. This reflects the smaller number of females born in the 1930's entering the major child-bearing ages.

Marriage and children are an important part of our standard of living. Developments during recent years suggest that, under favorable economic conditions, a part of the gains from increased productivity will be taken in the form of a higher proportion of married adults and more children per family. Just what part of such gains will be taken in this manner in the future is difficult to foresee.

More Children per Family

The growth in higher order births has resulted in a pronounced increase in the number of medium-sized families and since 1950 in the average number of children per family. During the 1940's, the average number of children under 18 years old per family decreased in spite of the high birth rate of that period. This grew out of the fact that measurements of average family size reflect births over a period of several years, not recent years alone, and the fact that the number of families was increasing at a faster rate than the number of children under 18. Since 1950, however, the continued development of families formed during and after the war has increased the number of children per family.

In recent years, the effect of this change in family composition has been influencing consumer demand. Two notable examples are the expanded demands for larger houses and for station-wagon type automobiles—both are related in part to the requirements of families with several children. These illustrations seem to be particularly good in indicating how the increase in our birth rate several

years ago is now affecting composition, as well as volume, of demand.

The most striking changes in the composition of our population have occurred in its age distribution. At the present time, there are more children under 14 and adults over 25 than in 1940. Fewer young people between the ages of 15 and 24 may be traced, of course, to the low birth rate of the 1930's. Some of the implications of this decline in terms of marriages and births have been indicated above.

The number of small children represents one of the most important population developments during recent years. The number of children under 5 years old increased 73 per cent and those between 5 and 9 years old, 61 per cent between 1940 and 1955. As a result, children under 10 years old now constitute over 21 per cent of our total population.

The influence of these youngsters on the composition of consumer demand for particular products and services may be observed in the increased volume and type of things, ranging from toys and breakfast cereals to specialized baby products and services, now available. As these young people grow older, additional modifications may be expected in the pattern of consumer spending.

The impact of this growth on schools also is generally well known. It is significant, however, to note that in mid-1955 there were well over 18 million children of preschool age (under 5 years); this is an increase of about one eighth from 1950. Most of these children will be entering school during the next five years.

Enrollment in elementary and high schools will continue to increase rapidly during future years. Elementary grades will sustain the major part of the increase, although high school enrollment also will increase rapidly. The peak growth rate in high school enrollment will come in the early 1960's when the large elementary classes of this decade progress to that level. In broad terms, there will be four high school students by 1960 and five by 1965 for every three today.

On the other hand, the number of persons of college age (18 to 24 years) declined between 1950 and 1955.

(Continued on page 42)

The Economics of Sale and

THE ownership of stocks, bonds or other securities of a corporation does not require the owner to devote his time and energies to the management of the corporation's business. He has nothing to do except to receive his interest or dividends but this isn't so with the ownership of usual or conventional income real estate.

The owner of an apartment house has to manage it or delegate someone else to do it. He has to look after the upkeep, repairs and maintenance, collection of rents, purchase of supplies and payment of taxes and insurance. From time to time he may be required to obtain tenants to fill vacancies, frequently at an expense and also after loss of rentals.



David B. Gadlow

Likewise, the owner of an office building has similar responsibilities. He must employ and supervise his personnel. He must pay their wages and social security contributions, as well as keep books and records, just as for any other business.

The owner of a hotel, especially a large one (unless he leases it to an operator) has to conduct a business comprising a multiplicity of departments. The degree of the success of the enterprise, like most businesses, depends to a great extent upon the ability and quality of the management.

Owners of such properties, as well as of store and other commercial properties, are engaged in the business of merchandising residential and commercial housing and their related services. For obvious reasons, these owners are usually required to reside in close proximity to their properties.

But there are at least two types of real estate investment which correspond more closely to the ownership of corporate securities in that the owner or investor is relieved of man-

agement responsibilities and therefore not restricted to the locale of his residence. One of these, frequently termed a "ground-leased fee," is the ownership of land ground-leased for a long term on which the lessee has erected substantial improvements, having a value sufficiently adequate to secure the ground rentals. The lessee usually is required to pay the taxes on the land, as well as on the building, in addition to insurance and all operating expenses. The building is pledged as the underlying security for the ground-lease. In the event that the lessee defaults on its lease obligations, particularly payment of rentals, it may forfeit the building which then reverts to the owner of the land. Some recent notable examples:

Several years ago Prudential purchased the land under the Empire State Building in New York and simultaneously entered into a long term ground-lease with a corporation which purchased the building.

The Russ Building in San Francisco was erected on leased land. In 1926 the Russ Estate Company which owned the land entered into a 99-year ground-lease, as lessor, with the Russ Building Company, as lessee. The latter erected and owned this 30-story office building. A few years ago, the Russ Building Company purchased the land from the Russ Estate Company. Recently, the property (both land and building) was sold for approximately \$11,500,000 — at this price the improvements represented almost three times the value of the land. This indicates the margin of safety which the land owner had.

Another type of a secured realty investment is one in which both land and building are subject to an absolute net lease for a long term of years to a tenant of prime financial standing. In this instance, the owner is relieved of the ordinary cares and responsibilities of management incident to the ownership of conventional income real estate. As in the case of corporate securities, the owner has nothing to do but to receive his

monthly rent check. Properties, so leased, are attracting non-resident investors, particularly institutions such as life insurance companies, universities, pension funds and church organizations, as well as banks and other custodians of trust funds.

An absolute net lease is one wherein the lessee pays the same real estate expenses as if it owned the property, namely, taxes, insurance, repairs, maintenance, operating costs and any and all alterations and improvements. The term "absolute net lease" derives from the fact that the rentals received by the owner are net, or free, of all real estate expenses.

During the 1930s, life companies, like other mortgage lending institutions including banks, acquired considerable real estate through foreclosure. Many were not equipped to manage the real estate so acquired. Some had to form their own property management departments. Others placed their properties with real estate or mortgage firms which had experienced organizations to manage them. The companies were required by law to divest themselves of these properties within a specified period, usually five years, unless extended by the Superintendent of Insurance or other state insurance authority. As favorable opportunities arose, the properties were sold and liquidated. Obviously many of these companies would not be eager to purchase conventional income-producing real estate for investment, if and when they could legally do so.

About 1937, I suggested to an attorney in San Francisco that life companies might be enlisted to support legislation permitting them to purchase commercial real estate for investment. At that time they could legally purchase only a home office building and, in certain states, "real estate for the convenient transaction of its business." Under this latter provision they could purchase a branch office building. Nothing came of my suggestion, however.

Lease-Back Transactions

By DAVID B. GADLOW

Not long ago someone pointed to the shopping center as the only really new development in real estate during our time—but it wasn't quite true. The sale and lease-back transaction is new, but not quite as new as most of us think. Mr. Gadlow recalls one of more than a quarter-century ago which met the requirements of a present-day transaction but, because of unusual circumstances, didn't become a deal. What is back of a sale and lease-back deal, what do both parties expect to accomplish, what have been the real reasons why such a vast amount of investment money has gone into these transactions—and what, particularly, is the role played by tax savings? That is what Mr. Gadlow does here—look into the economics of the sale and lease-back transaction. He is a good one to do it because, by some, he is credited with being the creator of the transaction (credit which he modestly disclaims, however).

About three years later, a representative of the real estate department of Safeway Stores, Inc. proposed to me that I submit his company's properties, on a sale and lease-back basis, to life companies. I told him that life companies could not legally purchase commercial real estate for investment.

Subsequently, in 1941 and at a time when these companies, like others, found it difficult to invest their increasing and surplus funds in sound and safe investments which would earn an adequate yield, Virginia broke the ice and amended its investment statute so as to permit life insurance companies of that state to invest up to 5 per cent of their total admitted assets in the purchase of commercial properties. This enabling legislation became effective January 2, 1942. On that day, The Life Insurance Company of Virginia bought a produce warehouse in Washington, D. C. from Safeway Stores on a lease-back basis.

North Carolina adopted similar legislation in 1943. A number of other states followed suit, including New Jersey and New York. At present more than forty states and the District of Columbia permit life insurance companies to invest a portion of their assets in this manner. As a result of this legislation, approximately two billion dollars became available for the purchase of commercial real estate by such companies.

The establishment in recent years, by business and industry, of employees profit sharing and pension funds, augmented the stupendous sums which could be so invested. At no other period in the history of this country was such an astronomical sum allocated for the purchase of real estate.

Life insurance companies have invested \$1,297 million in commercial properties up to December 31, 1954.

With the passage of this enabling legislation, Safeway Stores took the greatest advantage of this unprecedented opportunity to finance, through the sale and lease-back method, its store, warehouse and other properties. This company led all others in the volume of real estate which it sold in this way. It is reported that the aggregate of such Safeway sales, including pending commitments, is between \$350,000,000 and \$400,000,000.

Eventually, other companies throughout the United States and Canada adopted the sale and lease-back plan. These included General Motors, General Electric, Western Union, Sears, Roebuck, Continental Can, Remington Rand, R. H. Macy, and a host of others.

A number of innovations have been introduced into sale and lease-back transactions. One is the provision giving the vendor-lessee renewal options at rentals substantially below those provided for during the initial or pri-

mary lease term. This provision evolved out of the following circumstances:

Life companies, universities, pension funds, churches and other institutions did not wish to own conventional income real estate, with the cares and responsibilities of management and the uncertainties of assured and sustained income over a long period of years. Many life companies and other mortgage lending institutions had had their fill of this type of real estate acquired through foreclosure. They now wanted to own property subject to an absolute net lease with a corporation of acceptable financial standing for a term generally ranging from 20 to 30 years, at rentals sufficient to amortize their entire investment in both land and building during this period and, in addition, provide for a satisfactory rate of interest.

This was indeed a revolutionary departure from the customary and traditional concept of income real estate ownership. Owners of such real estate usually expect to have a substantial part of their investment in property after lease expirations, particularly where leases run for a comparatively short period of years.

To meet the special formula set up by these institutions, it was necessary to obtain a higher rate of return than the commercial real estate market was then affording. Choice retail proper-

ties, under long-term net lease to chain store companies of prime credit, were then selling at prices yielding an over-all return of from $4\frac{1}{2}$ per cent to 5 per cent net and, in some instances, even less. This low return would not permit these institutions to realize their principal amortization and interest requirements within the primary lease term. Therefore, as an inducement for a prospective vendor-lessee to pay rentals sufficient to meet such requirements, these institutions offered to such vendor-lessee certain compensating future benefits, in the form of an option, or a series of options, to extend the lease for varying periods (in some cases stretching well into the next century) at substantially reduced rental rates.

These reduced rental rates during the renewal periods were devised to meet the particular amortization and interest requirements established by the institutional investors.

It is hardly to be expected that any corporation of select financial standing will sell its property (particularly one having a comparatively new building and a substantial residual value at the end of the primary lease term of from 20 to 30 years) and pay rentals during this period sufficient to return to the purchaser its entire investment, with interest, without attaching strings in the form of renewal options at rental rates substantially below those provided within such primary lease term.

Consider an actual case where the rentals during the primary lease term of 25 years is equal to 6.67 per cent per annum of the sale price. These amounts are sufficient to amortize the purchaser's total investment over this period with interest at $4\frac{1}{2}$ per cent per annum. Thereafter the vendor-lessee receives a series of options to renew the lease for additional periods at an annual net rental equal to 2 per cent of the sale price. It amuses me when I occasionally hear a representative of an institutional investor say, "We don't like these cheap renewal options." Such renewal rates, which are generally based on a percentage of the original sale price rather than the owner's actual investment, may not be as "cheap" as they appear.

In its earlier real estate sales, Safeway generally allowed a purchaser, in addition to interest, amortization merely on the building. Suppose a warehouse, plant or industrial property was sold on this basis for \$1,000,000, of which the land represents \$100,000. Accordingly at the end of the primary lease term, the purchaser would have a remaining investment in the property of \$100,000. Assume that the vendor-lessee has a series of renewal options at annual net rentals equal to 2 per cent of the total sale price of \$1,000,000. Such renewal rentals, then would amount to \$20,000 a year. This amounts to an annual yield of 20 per cent of the purchaser's remaining investment of \$100,000.

Now consider a common transaction where the rentals, during the primary lease term, are sufficient to amortize the purchaser's entire investment with interest—say all but \$1 of this investment. Based upon a renewal rate of 2 per cent of the total sale price of \$1,000,000, the purchaser will receive as rentals, during the renewal periods, \$20,000 a year on an investment of \$1. This is equal to an annual yield of 2,000,000 per cent on the investment! It sounds utterly fantastic, doesn't it? The amazing thing about these figures is that they are not only mathematically correct, but are an actual fact if the purchaser amortizes, from the rentals received, all but \$1 of its total investment. Of course these percentages, while true, could be misleading unless taken into consideration with the investor's over-all yield on the total original investment.

Following the enactment of the enabling legislation by Virginia and North Carolina, I communicated with principal life companies of these states, several of whom had already purchased Safeway properties on a lease-back basis, inquiring if they were interested in the purchase of additional properties along these lines. They advised that they were. I wrote real estate brokers in various parts of the country inquiring if they had any properties for sale which were subject to a long-term net lease with corporations of choice credit. The replies disclosed that properties with such leases were closely held by individuals and other owners and were not for sale except at prices that produced a yield which was entirely inadequate to meet the amortization and interest requirements of these life companies.

I realized then that, in order to meet such requirements, a lease would have to be "tailored to suit." This might be achieved, I reasoned, by interesting a company whose financial standing, as a lessee, would be acceptable to these institutions, to sell real estate which it owned and occupied and simultaneously take back a long-term net lease thereon. The company would thereby become a tenant-occupant instead of an owner-occupant of the property. This would enable it to convert fixed assets into working capital which might be employed more profitably in its business.



Accordingly, I addressed a letter to a number of nationally known corporations inquiring if they would be interested. Among the replies was one from Lerner Stores of New York, advising that it would consider such a sale on a new building which it owned and occupied in Atlanta. I inspected the property and later sold it to Jefferson Standard. Lerner took back a net lease for 30 years. The sale price was \$210,000. Jefferson Standard was pleased with this purchase and informed me that they would be interested in additional investments of this character.

I now embarked upon a national campaign to interest other corporations in the sale and lease-back of their real estate, which was to culminate several years later in the largest transaction of this kind, from the standpoint of sale price, of a single parcel of property.

Greyhound Corporation of Chicago was another which responded. The upshot here was that I sold for one of its subsidiaries, Southwestern Greyhound Lines, Inc., its new bus terminal in Houston. The purchaser was the Baptist Foundation of Texas. Southwestern Greyhound took back a lease for a primary term of 25 years with a series of renewal options for extended terms at substantially reduced rentals. The sale price was \$850,000.

Another Chicago company responded, Spiegel, Inc., well established mail order and chain store concern. This resulted in my sale for this company of four properties in Chicago at a price aggregating \$3,380,000. One was a retail store building, the others large warehouses in the Central Manufacturing District. The purchaser was Woodmen of the World in Omaha. Subsequently, I also sold for Spiegel, on a lease-back basis, two parcels of property in Kansas City to Yale University for \$1,000,000.

I also introduced this form of sale and lease-back transaction to Butler Brothers. This resulted in my selling a small property for this company in Cleburne, Texas. Later I sold a 12-story building for them in New York for \$850,000. In each of these sales, Butler Brothers took back a long-term net lease with a series of renewal options.

The Fulton Bag & Cotton Mills of Atlanta also replied. This resulted in my selling, on a lease-back basis, a new building for this company in Dallas for \$450,000. The purchaser was the Relief and Annuity Board of the Southern Baptist Convention.

During 1943, I learned of two properties in Manhattan, which already had the lease feature desired by institutional investors. The properties, which were under one ownership, were subject to long-term net leases with the F. W. Woolworth Company. One of these was an 18-story store and office building at 33 West 42nd Street; the other was a multiple store structure uptown.

I sold these properties in 1945 to Thompson-Starrett for \$8,250,000. The following year I resold them for Thompson-Starrett, to Yale University for \$9,350,000. The properties were then subject to certain loans. Following the enactment by Congress in 1950 of a tax measure, which affected the exemption of rental income received by universities, charitable organizations, and other eleemosynary institutions, which was used to retire a mortgage loan or other real estate indebtedness, Yale paid these loans and sold an interest in the properties, on a free and clear basis, to a group of pension funds.

Another company which responded was Western Union. This culminated in the sale in 1948 of the company's 24-story home-office building in New York to the Woodmen of the World

for \$12,500,000. This was the largest sale, from the standpoint of sale price, of a single parcel of property which had been sold on a lease-back basis. Western Union took back a lease for a primary term of 25 years, with a series of renewal options aggregating 75 years more.

In some quarters I have been credited with being the author of the sale and lease-back plan but this is not so. I have disclaimed credit. Safeway made the first sales of its real estate to life companies, following the enactment of permissive legislation. However, it may be said that I was the first real estate broker, following such legislation, to initiate and embark upon a campaign to interest other corporations in the sale and lease-back of their properties.

Gradually, as other real estate brokers throughout the country became aware of this development, they joined in the solicitation of corporations for the sale and lease-back of their properties. Mortgage loan firms and a number of investment securities houses also picked up the trail. In some instances, life companies and other investing institutions made contact directly with corporations for this purpose, and vice versa. Hardly any corporation of suitable financial standing was overlooked. Indeed, most of them were besieged from many quarters with the same proposal!

The enormous amount of capital required by the large corporations of this country for post-war construction of new buildings, and other facilities



ties, greatly stimulated this form of realty financing. The wave of sale and lease-back transactions which ensued, and the publicity which accompanied them, caused a great deal of comment and speculation as to the reason which brought it about. Those unacquainted with the facts, including some writers for tax and other publications, jumped to the popular but fallacious conclusion that income tax consideration was the motivating force behind the movement. The belief was even echoed in Congress.

When a company sells its property on a lease-back basis, it is merely exercising the prerogative of any per-

son, firm or corporation in this country to occupy its business premises as a tenant or as an owner. Had the company leased its property at the outset instead of owning it, nothing would have been said about it. Then why so much ado about income tax motivation just because an owner-occupant elects to change his position to that of a tenant-occupant? In what conceivable manner does a vendor-lessee enjoy any tax benefit, as a rent payer, which is not enjoyed by all other commercial rent payers?

While it is true that income tax is a very important consideration in almost any large business transaction, and that there may be certain income tax savings from the payment of rents, the fact remains that this was *not* the principal and underlying incentive of the vendor-lessee in most of these sales. If the income tax laws were repealed tomorrow, I am confident that these sales would continue, so long as substantial funds are available for this type of investment at

attractive rental rates to a vendor-lessee. As long as a corporation can employ its capital in its business at a higher return than rental interest rates charged by institutional investors, there will always exist a sound economic reason, independent of income tax considerations, for such company to lease rather than own properties required in the conduct of its business. This is true, provided that the company can secure its occupancy under a lease for a sufficient length of time and upon proper terms. In some cases, it might be desirable and even essential for the vendor-lessee to receive an option whereby it

may ultimately repurchase the property. There have been a few isolated instances where corporations have sold their properties on a lease-back basis in order to take advantage of tax losses. In such cases the properties were carried on the books of the company at prices substantially above their market value. The sellers, of course, were required to substantiate, by competent appraisals, that the sales price coincided with the market value. These transactions were the exception rather than the rule.

I recently wrote a number of corporations which have effected the sale and lease-back of their real estate, expressing my views and requesting them to state the primary reason which motivated them in making such sales.

John F. Lebor, vice president of Federated Department Stores, Inc., which operates a chain of major department stores, including Abraham &

Straus and Bloomingdale's of New York, Filene's of Boston, F. & R. Lazarus of Columbus and others, replied:

"During the last nine years we have effected sale-lease back transactions on more than 15 properties where the aggregate sale price exceeded \$75,000,000. Basically, these transactions reflected the method we used of arranging to occupy new facilities under a leasing arrangement. Like most other retailers, it has been customary for our company to lease most of its real estate because our merchandise selling prices and profit margins do not produce an adequate return to justify large investments in low earning assets such as real estate. To have a competitive, dynamic retail business, one needs to turn his capital frequently because of the low profit margin on sales customary to the industry. . . .

"Sale and lease-backs in varying forms have occurred for decades. It has been the rapid growth of our economy and the enactment of new legislation to broaden the number of real estate investors that, in my opinion, has basically increased the activity and literature in this field.

"Too many people have the impression that a lease resulting from a sale-lease-back transaction is something different from a lease in which the title of the property was never in the hands of the lessee."

L. A. Ahlers, treasurer of Western Union, wrote:

"... regarding sale and lease-back transactions, I agree in principle that they are justified quite apart from income tax considerations, if investment funds are available at attractive rates and can be used profitably without endangering the future by unjustified long-term commitments.

"So far as Western Union is concerned, each sale and lease-back transaction was undertaken on that basis, namely, the economic benefit available therefrom."

Graham Magee, vice president of Lerner Stores, wrote:

"Retailers are retailers and they have no reason to keep funds invested in real estate; such funds must and should be available for corporate as well as for expansion purposes. In-

"Income tax or no income tax, there are other reasons which impel corporations to sell and lease-back their company-owned-and-occupied properties. Officials of a corporation who would not think of employing their company's capital in long-term investments at institutional rental rates may not realize that they are in effect doing that very thing when they elect to own—when they can lease—properties required by the company. To the extent the company has its funds tied up in such properties, to that extent it is competing with institutional investment rental rates in the employment of its capital."

come tax provisions had nothing to do with our plans to dispose of real estate and the taking back of long term leases."

M. E. Arnett, vice president of Bullock's, Inc., Los Angeles, said:

"Taxes, definitely, are not the controlling element. The controlling element, in our opinion at least, is the opportunity to control the real estate we occupy, and enjoy a fixed commitment at a reasonable rate of interest with an opportunity to enjoy even more favorable rental rates in renewal periods when building replacements and improvements must be made.

"Including the period of renewal we enjoy also all of the benefits of complete ownership without many of the burdens."

James E. Burd, treasurer of Spiegel, Inc., had this to say:

"The primary reason which motivated Spiegel, Inc., to effect the sale and lease-back of certain store and warehouse properties which were acquired during the past ten years was management's desire to employ the required moneys as working capital rather than to freeze these funds in fixed assets. In our mail order business there is a constant requirement for liquid funds to finance merchandise inventories and a very substantial accounts receivable asset.

"Under the circumstances, we make every possible effort to avoid committing major capital funds in plant outlays since our studies and experience clearly indicate that use of these funds as working capital is more profitable than diversion into fixed assets. I might add that the principles underlying this financial policy have not been born out of tax considerations but stem entirely from the growing need for adequate working capital."

These statements substantiate my contention that, income tax or no income tax, there are other reasons which impel corporations to sell and lease-back their company-owned-and-occupied properties.

Officials of a corporation who would not think of employing their company's capital in long term investments at institutional rental rates may not realize that they are in effect doing that very thing when they elect to own—when they would lease—

properties required by the company. To the extent the company has its funds tied up in such properties, to that extent it is competing with institutional investment rental rates in the employment of its capital.

After all, is it not the principal purpose of a company, in owning property which it occupies, to assure its continued and uninterrupted occupancy of the property? If this can be accomplished through a long-term lease, with adequate renewal options and, where essential, with an option to ultimately repurchase the property, why tie up the company's capital in this manner?

would reflect the depreciated cost of such real estate in its assets, while its liabilities would show the amount of such additional outstanding loans, which of course would be very considerable—possibly as much as \$300,000,000, if not a great deal more.

Since the leasing of properties obviates such loans, which ownership may necessitate, is this not a good and sufficient reason why a company, particularly one occupying considerable real estate, should lease rather than own its properties?

Comparisons have been made of the relative advantages and disadvantages, from income tax and other

"It may be asked whether the quality of the security in such (sale and lease-back) investment is as good or better than the usual mortgage loan. My answer is that I do not know, nor have I heard, of a single instance where a life company or other institutional purchaser of commercial properties, so leased, have suffered any loss during the past thirteen years through the default of a lessee in the payment of rentals. Considering that substantially more than \$1.250 million have been placed in this type of investment during this period, does this not, at least in a good measure, answer this question?"

In referring to accounting practices in the treatment of contingent rentals under a long-term lease in a corporation's financial statement, several have pointed out that it is not common practice to capitalize rental obligations and that, as such, they do not appear as a capital liability in the statement, as would a loan. Treasurers and other officials of corporations are well aware of the importance and value of a company's statement reflecting as small a ratio as possible of loans to capital assets.

Suppose Safeway had chosen to retain the ownership of the vast and unprecedented amount of real estate which it sold on a lease-back basis and had, instead, financed the total cost of such real estate through the issuance of long-term debentures (assuming, for the purposes of this discussion, that the company, in addition to its other loan requirements, could and would have financed these properties in this manner). In that case, Safeway's current financial statement

standpoints, between the financing of real estate through sale and lease-back and a direct corporate loan. One analyst points out a significant advantage which leasing has over debt financing. Have you ever read a corporate loan agreement? They contain various and sundry restrictions on the borrowing corporation—restrictions not found in a lease.

Having pointed out the principal advantages to the vendor-lessee in such transactions, someone may ask, "What are the advantages to the vendee-lessor?" The purchase of commercial real estate subject to such a lease affords the investing institution a distinct and profitable advantage. The investor ultimately receives, in addition to the return of its entire investment with interest, the residual value of the real estate plus whatever rentals are paid by the lessee during the renewal periods.

It may be asked whether the quality of the security in such investment
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FOR FHA'S COLLEGE HOUSING PROGRAM WE NEED

A REALISTIC INTEREST RATE

By JOHN C. HAZELTINE

FHA's college housing program isn't going to get off the ground—with 40 and even 50 year loans at 2¾ per cent. The program is wisely conceived, says Mr. Hazeltine, but the artificially low interest rate eliminates private participation in the financing. Mr. Hazeltine sets forth the arguments as to why this section of the law must be changed if it is going to work as Congress intended—and what makes all this even more interesting is that Mr. Hazeltine is Commissioner of HHFA's Community Facilities Administration and addressed the same arguments to the Council of Presidents of Land Grant Colleges and Universities.

APPPLICATIONS under the FHA college housing program have been flooding in since the enactment of the new legislation. Estimates of funds needed for the current fiscal year for such loans become out-dated almost overnight. This has posed a serious fiscal question, but a decision has been reached at the top levels of the Administration which will permit this program to develop without budgetary limits to the full extent authorized by the law.

This does not mean that the program will not be tightly administered; on the contrary it must be administered even more tightly than before. It does not mean that funds are unlimited; on the contrary, it will be necessary to scrutinize applications more closely than before. Only the most pressing of needs can be satisfied. However, it does mean that there has been full recognition of the size of the problem facing our educa-

tional institutions and that this Administration is prepared to carry out to the fullest the authorization provided by Congress.

Some serious problems arise from this decision. I am taking an unpopular position and arguing that this legislation over-reaches itself on one cardinal point. I maintain that the artificially low interest rate, and the resultant discouragement of private participation in the financing of residence hall construction, is against the best interests—the long-term best interests—of our educational institutions. I contend the program is on unsound ground at this point. I am going to ask educational institutions to join with the Administration in its efforts to obtain a more reasonable approach to the interest rate in order to encourage more private participation in this program.

In other words, I am going to attempt the Herculean task of asking

the borrower to understand the position of the lender. Psychologically this is like trying to make water run up hill. But in this case it is not quite as paradoxical as it may seem—because while you (the educational institutions) are the borrowers, you are also the lenders—as taxpayers and the leaders of a group which I firmly believe is the strongest champion we have in this country of orderly administration and of our efforts to curb inflationary tendencies in the national economy and to balance the federal budget.

Clarence Randall emphasized in his speech to ABA last Fall that many business men who have attested their fullest approval of President Eisenhower, have failed to support his policies or, at best, have given them only lip service.

Many who appreciate fully the needs for inflationary curbs on our economy and who understand full

well the importance of a balanced budget, have nevertheless faced this Administration with a tremendous problem. Educational institutions have appraised us of their estimates of two to three billion dollars in educational housing needs over the next few years—while favoring an interest rate which can only mean that whatever loans are made under this program will necessarily remain direct federal loans to be included in the annual disbursements from the federal budget. Sums of this magnitude should come primarily from the private investment resources of the nation rather than from the federal government.

Now I can anticipate the comment that federal loans to colleges and universities are investments and not expenses. In fact, one college president said to me, "Any bank that carried its loans as disbursements would show one hell of an annual statement." He is right, of course. These college loans are not truly expense items. They do, however—and we must face it—represent at this stage an annual net outgo from the Treasury and to that extent they must be funded, either through taxes or borrowings, precisely as any federal expense.

What is the answer? It is that we must present to the Congress the basis for a more equitable interest rate and one which will make it possible for the greatest proportion of these loans to pass into the hands of private investment.

I want to warn that the program

is vulnerable as it stands. It is vulnerable from the standpoint of carrying a subsidized interest rate. We can rationalize all we want about long and short term rates and about the average rate of total federal borrowings being below the college housing interest rate, but the plain fact is that when the federal government needs long term, say 30 year money, it has to go out and pay at least 3 per cent for it. Yet under the new law the loans to colleges for 40 and even 50 years are at 2¾ per cent.

That simply isn't a logical proposition and no one can refute the people who say that a subsidy is involved. This is already apparent in Congress where bills have been introduced in both houses to abolish the college housing program. Other bills have been introduced which will raise the interest rate far above anything I would propose. Measures of this kind will gain support if we cannot defend a balanced program in which the largest proportion of these loans can be channeled into private investment. Although we are all agreed that college housing loans are sound investments in institutions which are central to the very core of our national existence, this valuable program may be lost if it can be made to appear by its opponents as a greedy grab for Federal funds at a time when all reasonable people recognize the need for restraint in Federal disbursements—even for restraint in investments of this high caliber.

So get down to specifics, exactly what is the difference between a loan at 2¾ per cent and a loan, say at 3¼ per cent, a rate which should attract a substantial amount of private investment? Assuming a per bed cost of \$3,000, the difference in interest rate amounts to just \$10.32 a year, or \$1.14 per month on a nine-month basis—only 86c on a 12 month basis.

This is the small differential which stands between a direct federal loan and an offering which would be more attractive to the public.

I am not advocating high rentals in residence halls. What I am arguing is that the minor adjustments involved, because of that differential between a 2¾ and 3¼ per cent rate, are not going to be an appreciable burden either on the student or the institution.

There are also some intangibles involved in this problem which must be considered. I am talking now about the close relationships which have been built up over the years by educational institutions with the banks, insurance companies and investment firms which have been supplying their needs for capital. By and large, the schools have been obtaining prime rates, with a minimum of red tape and quick and sympathetic consideration of their needs. I believe that they should think long and carefully before breaking those ties for the purpose of obtaining a small reduction in interest rates. These lenders are friends of our schools whose influence and

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► A Look into the Future ► For the Mortgage Industry

► **By Clarence J. Myers**
President, New York Life Insurance Company

► In Mr. Myers' forecast for tomorrow in the mortgage industry, and for the general economic health of the nation, there is no room for pessimism or doubt. The future is what we make it and all the tools for even better times are available for us to use. But change is one thing we can always count on, and there will be changes—for example, in the character of mortgage lending. Life company holdings of mortgages, he observes, have risen from 15 per cent of total assets to 32 per cent in ten years—and we can hardly expect them to go up another 17 per cent in the next ten years bringing holdings to nearly 50 per cent of total assets.

TO SOME extent insurance companies are direct investors in real estate, but their main interest arises through mortgage loans.

Occasionally there arises some misunderstanding about what they can



Clarence J. Myers

do, or are trying to do. This is an important thing, because the life insurance industry now owns \$2½ billion in real estate and \$28 billion in mortgages. Life companies loom large in the mortgage field. In recent years they have contributed about one-fourth of the total mortgage money that is used in financing the real estate sector of the American economy. Their contribution attracts considerable attention for two other reasons: their mortgage money goes largely into the financing of residential real estate—homes for a representative cross-section of the American people. And of course housing is a very personal thing—everybody is concerned with its cost and its availability. For another thing, construction activity is largely dependent on

mortgage financing; and general business activity is affected to an important degree by the incomes and demands generated in the construction industry.

For these reasons, when life companies invest money in mortgages, they are conscious that our actions affect the public in many important ways, directly and indirectly.

The life companies have aggregate assets of \$88 billion, one-third of which has been used to buy mortgages and the balance is in securities, chiefly bonds of companies furnishing transportation, communication, public services, or engaged in manufacturing or production of raw materials.

Life companies furnish a livelihood to 380,000 men and women as employees or agents. Four out of five families in the United States have one or more policies. In North America the ownership of life insurance is \$1,900 per capita and our nearest rival is England at \$400 per capita.

Premiums of \$11 billion are paid annually for this protection. Until such time as the money is called for under the terms of the policies, the life companies hold this money and invest it.

So fundamental is the character of our business that we can project with relative accuracy the flow of funds to us and hence we are able to make with confidence commitments to furnish money for future construction.

Also, because of the size and constant growth of our assets we can put more emphasis on the safety and yield of our investments than on their ready marketability.

Our aim is to get the best combination of security and rate of return but, because of our size, we must also act with an awareness of our influence upon the economy as a whole. After all, we in the insurance business are the trustees of 93 million policy owners and our gain cannot be at their expense. We are an inseparable part of the economy in which we operate.

Some misunderstandings which occasionally arise in connection with the investment of life funds, and particularly with regard to mortgage investments, are:

One area in which a misconception is apt to be found is that relating to the in-flow of our funds. For example, those who are impressed with the way our funds support economic development sometimes talk as though we in

the insurance business can control the total volume of these funds. Of course this isn't so. The cash flow of life insurance companies is simply part of the savings of the American people. We do not determine this flow. We have available for investment only as much money as policy owners entrust to our safekeeping. That is a relatively fixed amount, and it is not of our choosing.

A second area of frequent misunderstanding relates to the distribution of this investment money. There is a tendency to overlook the driving force determining that distribution. We live in a highly competitive world. There are over 1,000 life insurance companies, all acting independently. They face an ever-changing set of competing demands for their funds. Consideration must always be given to the relative attractiveness of putting money into bonds, stocks and mortgages, to the relative merit of loans for housing, for expansion of chemical factories, for power plants, toll roads and so forth. As conditions change, mostly represented by changing yields, the distribution of funds is bound to change.

There is no more striking example of the fact than in the mortgage field since World War II. In 1945, as a result of the wartime blackout on residential construction, mortgages represented only 15 per cent of the life companies' assets. Today, ten years later, the proportion of assets invested in mortgages is about 32 per cent.

This is an extraordinary change. And it is perfectly clear that such a change was made possible because the life companies had abnormally large holdings of government bonds that could be disposed of after the war and thus provide a source of cash. To be specific, in 1945 we had 46 per cent of our assets invested in U. S. government securities. Today, with the government's need for financing a less urgent one, the proportion of assets in government securities is down to 10 per cent. Thus, during this decade our government holdings have decreased by \$11½ billion and our mortgage portfolios have increased by \$21 billion.

This period of readjustment has ended. Sale of government bonds can

no longer provide substantial funds for purchase of mortgages and other private investments. From now on, it might be expected that the expansion of each form of investment will more nearly depend on the competitive division of the net growth of total assets. The truth is that we won't have as much money for mortgages and the amount finally invested will depend to a large extent on how they score in the final measure of safety and yield.

The third area in which there may be need for a clearer understanding is that pertaining to the influence of government policy on mortgage financing. Let me cite two examples of strong government influence.

There was the unpegging of the government bond market in March of 1951. Prior to that date the Federal Reserve System had been supporting the government bond market at prices above par. The life companies, having large holdings of governments, could purchase mortgages in exchange for bonds to be sold at par or better. There was no need to watch the cash flow. Unpegging the market cut the availability of mortgage funds sharply, both because the companies were reluctant to sell governments at a loss and because, as credit generally tightened, yields on corporate bonds became more attractive than the relatively fixed rates on FHA and VA mortgages.

In the summer of 1953 the situation changed as certain steps were taken by the Federal Reserve Bank to make credit easier. Declining yields on bonds made mortgages relatively more attractive. Most important, government regulations were changed to permit rates of interest on mortgages to become adjusted to competitive levels. The result was a heavy flow of funds into the mortgage market, which gained momentum lasting into 1955. With business recovery toward the end of 1954, bond yields began to move up again; but this time mortgages could hold their own in competition with other securities because of the flexibility of yields on FHA and VA mortgages—a policy, incidentally, that we in the life insurance business have long advocated.

In early 1955 the Federal Reserve began a series of steps designed to tighten the terms of credit generally. In July, both the FHA and the VA

raised down payment requirements and reduced maximum payment periods. With demand already running ahead of the supply of funds, the tightening of mortgage credit terms was inevitable even in the absence of government intervention. The government's actions largely put an official seal of approval upon what the market was already inclined to do.

The emphasis which government authorities have placed in recent years on flexibility of interest rates is most desirable. Conditions in the capital markets should be determined primarily by supply and demand. Government policies should be directed largely to assist the natural interplay of those forces and to assure an orderly market. Rigidity is dangerous to the smooth functioning of our private enterprise system. The national economy is in much healthier condition today, by reason of this flexibility and freedom from direct government controls, than was the case during the first six years after the war.

Now, what is ahead—and when I say "ahead" I do not mean just immediately ahead. I think we should take a longer look.

I referred to the fact that the mortgage market during the last 10 years was dipping into a non-recurrent source of life insurance funds, the sale of government bonds. Here are some figures that illustrate that fact. During the last 10 years the assets of life companies showed a net growth of \$43 billion. It is convenient to think of this as new money seeking additional investments. Let us assume that we normally want to keep about one-third of our money in mortgages. If one-third of this new money had been used to augment our mortgage holdings, the latter would have gone up just \$14 billion during the 10 years period. Instead, our mortgage holdings actually went up \$21 billion. The extra \$7 billion, so to speak, was obtained by reducing our holdings of low-yield government bonds, which declined \$11½ billion during this period. The percentage position of mortgage holdings in our total assets rose from 15 per cent to 32 per cent during the past 10 years. We can hardly expect the next 10 years to witness still another rise of 17 per cent, which would bring mortgages up to 49 per cent of total assets.

Much of the demand for postwar housing was of a non-recurrent nature, just as the supply of money was partly non-recurrent. Construction during the past 10 years served in large measure to make up for the shortages that had accumulated during the war. Never in the history of our country have all levels of our society been relatively so well housed.

There is reason to expect greater stability of the flow of funds in the days ahead when terms of credit are flexible. Much of the "stop-and-go" driving on the route we traveled during the past 10 years reflected arbitrary limitations and interventions by government agencies.

We in the life insurance business are rather proud of the part we play in channeling a substantial share of the individual savings of millions of people into productive investments, both large and small, scattered throughout North America. We are also proud of the increasing skill with which we have been able to adapt the flow of our mortgage money to the intricate and fast changing pattern of demand for home financing.

Responsibility for the construction and financing of an adequate supply of housing is a real challenge for the housing and mortgage lending industries. With the fine cooperation that prevails today between government and our business, I think there is reason to welcome this challenge—to accept it confidently.

I am not a pessimist. In fact, taking a somewhat long look ahead, I see on every side grounds for much optimism. I believe we are now entering a new epoch of history. It will be a period of wonderful possibilities for progress. And we are entering this new era, I firmly believe, at a time when American business is better prepared than ever before to accomplish great things.

Some of the reasons for my being so convinced on this score are:

First, American productivity, which is the foundation for our well-being, has continued to go steadily up and up—and I fail to see anything which convinces me that it will stop going up in the years ahead. Also technology. Who can say where our horizons lie in this great field? We would be foolish indeed if we were to attempt

to predict the limit of discoveries still to come from our research laboratories in this atomic age. If production takes men, money and machines, how—looking at our labor supply and labor skills, our financial resources and our advancing technology—how can we be faint-hearted about this country's future capacity to produce?

Some, agreeing with me, may possibly have misgiving about the maintenance of our capacity to consume. I am just as optimistic about the demand side of the picture as I am about the supply side. We will occasionally have short periods of inventory readjustment, price readjustment, and readjustment to changes in the defense expenditure program. But how can we fail to have a strong upward trend in all the basic factors that create demand for consumers' goods and services?

The remarkable upsurge in the growth of the population is still continuing. The striking shift in the distribution of personal incomes has created a vast new middle-income market, whose needs are far from saturated. And every young couple to-day wants a higher standard of living than their parents and they will work in order that they can buy.

Two-thirds of all the dwelling units in the United States are over 20 years old and half of all dwelling units are over 30 years old! On the average, the age-distribution of our housing confronts us with a tremendous future market for replacement, or renovation, or both. This potential market won't materialize overnight. But for the long term, it gives us a tremendous backlog of consumer demand. It should be counted as one of the most important of the many sustaining forces that will keep our economy a dynamic and growing one in the years to come.

In summary, then:

» During the past decade, life companies contributed an abnormal volume of funds to the financing of postwar construction. Although there will be some tapering off, there is every reason to expect a continuation of mortgage investment on a scale that will support adequate housing and a healthy growth of the economy.

» It is encouraging to note that there is increased understanding and

cooperation between the government and the housing and mortgage lending industry. Greater reliance is being placed on competition in capital markets as an impersonal mechanism for allocating resources and regulating business activity. This bodes well for the productivity and stability of our economic system.

» The broad prospect before this country is tremendously stirring. There are many reasons for expecting vigorous economic growth and progress in the decades and generations ahead.

So I say "What a wonderful time to be living in!"

As condensed for an address before the American Institute of Real Estate Appraisers.

FHA's COLLEGE HOUSING

(Continued from page 31)

support come in divers ways besides the need for loans.

My case rests on these points:

- » The college housing program was wisely conceived, has met a real need and has deserved its expansion. The Administration is supporting it and backing it to the limits of the legislation.
- » The new legislation overreaches itself in the artificially low interest rate which eliminates private participation.
- » It is in the interest of the colleges and universities, as well as the federal government, to seek a more equitable rate which will encourage rather than discourage private participation.

Southern Statistical Company has acquired the schedule department of Investors Diversified Services, Inc., of Minneapolis, and has moved the operation to the Memphis headquarters of Southern. Southern Statistical offers amortization schedules, cashier and ledger cards and other products used extensively in the mortgage industry.

Southern will continue to serve the clients formerly serviced by Investors. Southern Statistical is under the management of James I. Elston, Jr., and the sales department is directed by W. W. Johnson. Hubert Alexander is office and production manager.

Martín on Credit and Físcal Polícies

(Continued from page 19)

year from commercial banks. Mortgage lenders have also been obtaining forward commitments from the banking system in order to be in a position to make good their own forward commitments to lend. A special survey of large city banks indicated that in the year ended August 10, loans of such banks to mortgage lenders had risen by over half a billion dollars and that additional commitments for \$1¼ billion of loans to such lenders were outstanding. In addition, direct real estate loans by commercial banks probably rose last year by over \$3 billion. It should be borne in mind that expansion in commercial banking operations creates new supplies of money in contrast to other financial institutions which lend existing funds.

Greatest House-buying Ever

It is evident that consumers have been buying houses—both old and new—at a higher rate than ever before. Builders' operations—which means houses under construction, builders' financial obligations, consumption of materials and need for credit—have been higher than ever before. Commitments of financial organizations to take mortgage loans have been very close to if not the largest on record. Moreover, a larger proportion of financial institutions appears to be obligated on commitments. This means that individual institutions have not had the freedom to respond to the current demands that they might otherwise have had. It no doubt accounts in part for reports that builders are unable to obtain additional forward commitments.

With the housing industry operating close to capacity and bidding actively against other industries for resources, prices of construction materials have increased. Properties under construction have been very high and so also has been construction financing to carry these inventories. The demand for funds has been beyond the supply of savings, and additional funds have been supplied from an unusually large expansion of bank credit.

Except, perhaps, for the extent to which commitments to finance future

transactions are outstanding, the situation in residential construction and real estate is very much like the credit situation generally. Heavy demands for credit have been in evidence almost everywhere—to finance the high level of consumer buying of automobiles and other durable goods; to finance business expansion of fixed plant and equipment; to finance public improvements by state and local governments. The federal government has also been a substantial borrower in recent months, but most, if not all, of this borrowing will be offset by debt retirement during the remainder of the fiscal year. The volume of investable funds becoming available from consumer and business savings has not been adequate to take care of all these demands. Mortgages are competing with all these other uses for the large, but limited, supply of funds.

While some expansion of commercial bank credit has been desirable in

order to supply additional cash balances, consistent with the growth needs of the economy, the commercial banking system could not have met all of these demands for credit not supplied from savings without running the risk of inflationary consequences.

In a prosperous, expanding economy, funds for financing home ownership, as well as financing ownership of other long-lasting capital goods, should come as far as possible from savings in the hands of the owners or made available on loan from institutional or other holders of accumulated savings funds. Free competitive credit markets are the most effective means for allocating these funds to applicants.

Under prevailing conditions, demands for funds are running far ahead of the supply of savings. To meet these demands by creating new supplies of money through the commercial banking system with Federal Reserve assistance, would invite dangerous inflationary repercussions throughout the entire country.

says George Dirks of McCord-Dirks Mortgage Co. in Indianapolis



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Problems Facing Savings Banks in Out-of-State Mortgage Purchases

By JOHN J. REDFIELD

One of the most important developments in the mortgage business in recent times has been out-of-state acquisitions by the mutual savings banks—indeed, without this development the story of the business of the past several years would have been quite a different one. But it has posed problems; so, if you are originator, step into the investor's chair and see what he has had to contend with in reaching out for loans beyond the customary sphere of his operations. For one thing, no two states have the same set of laws governing mortgage purchases. Legislation in some states presents investment hazards of considerable proportions. Mr. Redfield is with the New York law firm of Cadwalader, Wickersham & Taft and the foremost authority on the subject he reviews as he did for members of the National Association of Mutual Savings Banks.

WITH today's pressure for higher and higher interest or dividend rates on savings deposits, savings bankers find it increasingly necessary to discover new sources of high investment yield. Although mortgages have traditionally met this need reasonably well, many banks for the first time have found their local supply of acceptable mortgage investments inadequate and have begun to face the problems involved in the purchase of out-of-state mortgages.

The investment laws of most of the seventeen savings bank states have been liberalized, where necessary, to permit out-of-state investment in mortgages insured by FHA or guaranteed by VA. Out-of-state conventional lending is usually more restricted, where permitted at all, so these observations are limited to FHA and VA loans.

There are substantial advantages to an out-of-state mortgage investment program. It permits geographical di-



John J. Redfield

versification which helps to protect the bank against economic fluctuations affecting only one region or a few industries. It allows placement of capital in areas not already saturated. As a result, many banks have found it possible to purchase out-of-state loans at a considerably greater discount than that available locally, with correspondingly favorable net yields. Even disregarding a greater discount, the banks have found higher quality investments at comparable rates in areas where de-

mand for capital is greater compared with the home market.

Have these benefits been offset by disadvantages? Are the new problems involved too burdensome for the small or medium-sized savings bank to undertake? On the contrary, this field of investment has been found satisfactory by many smaller banks and the obstacles are by no means impractical to meet.

An out-of-state lending program raises three main legal problems:

» Compliance with local laws affecting the mortgagee's rights and remedies

» The question of "doing business" and exposure to local taxes

» Compliance with the requirements for maximum FHA insurance or VA guaranty.

To meet the first, that of local

mortgage laws and customs, the assistance of qualified counsel of the foreign jurisdiction is indispensable. There is a surprising variety of peculiarities of local law and custom which we have encountered in the some forty-odd states in which our clients have invested.

For example: Louisiana, besides requiring the use of unfamiliar civil law forms, accords a "privilege" to certain debts of the mortgagor's estate, such as funeral charges, support of an indigent widow, and expenses of last illness, which places them ahead of the mortgage lien, thus in effect making the lien a possible second lien. This can be avoided, however, if the mortgage is a vendor's lien mortgage and contains a clause so reciting.

The Texas constitution provides for homestead rights which are also ahead of the mortgage unless the mortgage represents a mechanics or purchase money lien. Title problems are raised, particularly in the Western states, by mineral extraction rights, which the investor must make sure do not carry with them a right of entry through the surface of the property.

In Puerto Rico you have some more civil law elements to deal with, as well as a mortgage in two languages, with the consequent necessity of assuring correct translation.

There are various forms of mortgage taxes in some states, usually coupled with the provision that the mortgage is not enforceable until the tax thereon is paid. In addition to the New York mortgage tax, there is an intangibles tax in Indiana which requires revenue stamps, and in Georgia, which requires a clerk of court's receipt.

Florida has a requirement that mortgagees must file with the State Insurance Commissioner a schedule of their requirements with respect to the acceptability of hazard insurance companies and agents, in order to enforce such requirements against the mortgagors. Some states, like Virginia, require no assignment of deeds of trust; some states, like Ohio, permit assignments by means of marginal notations on the mortgages; and some states, like Maryland, require an assignment when the security takes the form of a mortgage but not when it takes the form of a deed of trust.

Formalities of execution also differ. The absence of a notary's seal in New York is inconsequential but is a fatal defect in California and Texas. Texas requires a special form of acknowledgment for a married lady which recites that the nature of the document was explained to her "privily and apart" from her husband. Laws affecting fixtures and chattel mortgages also vary from state to state.

The cooperation of local counsel is necessary and there are also many varieties of laws affecting foreclosure, operation of foreclosed properties or local taxes. If a long range program is contemplated, the bank's general counsel should seek the basic opinion of local counsel regarding the requirements for a mortgage investment program, in so far as local law and custom are concerned.

Here are two examples of how subsequent advice from local counsel might affect the existing mortgage investments in the state concerned. In Michigan, following the advice of local counsel, we recommended that our clients qualify before investing in mortgages, even though such qualification involved a substantial risk of Michigan taxation and, in one case, involved payment of Michigan income taxes under protest and legal action for a refund thereof. In the middle of 1953 local counsel advised us of the passage of Michigan legislation permitting mortgage investment by unqualified foreign corporations in Michigan, the scope of permitted activities being broad enough to cover our clients' needs. We were, therefore, able to advise our clients to withdraw their previous qualification, thus eliminating the unnecessary tax exposure. In the beginning of 1955, local counsel in Texas notified us that the state legislature had enacted a law directing county clerks in counties having population of 600,000 or more to destroy all chattel mortgages and chattel mortgage records on file for a period of ten years or more unless within that period mortgagee's affidavits were filed to preserve these liens. Previously such chattel mortgages were effective until six years after the maturity date of the loan as set forth in the instrument. Because this law affected our clients' multi-family investments in Dallas and Harris Counties, we were able to

advise them to review such loans before the expiration of the ten year period in order to file necessary affidavits.

The next problem, the "doing business" laws in our sister states, is susceptible to some clarification. The question here has been whether the banks' activities in negotiating, acquiring, servicing, enforcing and realizing upon the security of their investments in these states, constitutes the performance of business therein and, if so, what penalties, fines or disabilities would ensue for failure of the bank to qualify in the foreign state, and what local taxation might be involved whether the bank qualified or not.

In general, direct lending by a bank in a foreign state is not practicable since it requires having employees and perhaps offices in the foreign state for that purpose. This involves additional legal and administrative costs. Where the enabling legislation permits out-of-state mortgage investment only if the mortgages are insured or guaranteed by the Federal agencies, there is also some doubt whether banks are thereby permitted to advance mortgage money on which the guaranty or insurance *will* be forthcoming only after the delay which is involved in presenting the papers to the applicable authorities for such insurance or guaranty. This, of course, does not apply to VA loans made on an "automatic" guaranty basis. More serious, however, it is generally held that such activity constitutes "doing business" in the foreign state. Even where no penalties are involved the liability for local taxation is usually greater. While a state may wish to encourage entry of new capital there is also an interest in protecting the local mortgage banking business against competition from outside. Mortgage investments are usually purchased from local originators, either on an "off the shelf" basis or by advance commitment. Formerly this latter method raised problems of compliance with VA and FHA discount regulations which happily are no more. But there is still the "doing business" aspect of this method to be watched. The arrangement must not constitute the local originator, merely the bank's agent for lending money in the state. The com-

mitment should be framed upon the assumption that the originator has already agreed to make the mortgage loans, and not conditionally upon the bank's commitment.

Unlike an individual, a corporation has no inherent right to carry on activities in a jurisdiction other than that in which it was created. Except for limited rights arising from the Interstate Commerce clause of the Federal Constitution, a corporation must seek the permission of the state in which it intends to carry on operations, if the state considers such operations as "doing business." Qualification, which is the term used for obtaining this permission, is not a complicated process and involves filing an application with the appropriate department of the state concerned and the payment of a usually nominal fee. The registration and payment of this fee generally must be repeated annually. In addition, arrangements must be made in many cases for the appointment of a statutory representative to accept service of process and other notices or, in some states, to designate the Secretary of State or other official to accept service of process in behalf of the corporation. Generally it is not necessary to obtain what is called a full qualification in order to purchase, service and enforce mortgage investments, as many states permit out-of-state banks to obtain a qualification which limits their activities to these matters. Few states, if any, permit an unlimited qualification by out-of-state banks, largely because the principal business of a bank is to accept deposits, which is not encouraged by sister states.

One thing has particularly concerned us: In some jurisdictions the penalties for the transaction of business in the jurisdiction by an unqualified foreign corporation are so severe as to deprive the corporation of its right to use the courts of that state to enforce contracts and, therefore, mortgages covering property in that state. This is an investment peril against which FHA insurance or VA guaranty offers no protection, since the investor claiming the benefits of FHA insurance or the full benefits of the VA guaranty must tender to the relevant Federal agency an acceptable title to the property, in the case of small residential loans, which title in

most cases would have to be obtained through court action. Even in large FHA loans where the defaulted mortgage can be assigned to the FHA Commissioner, a mortgagee may not avail itself of the benefits of FHA insurance in respect of a mortgage which cannot be enforced or foreclosed locally.

It is the current public policy of most states to seek to attract out-of-state capital. As a consequence there has been considerable legislation to facilitate investment by out-of-state corporations in local mortgages. This legislation takes the form either of defining permitted activities of unqualified foreign corporations as not constituting the doing of business, or of permitting some form of licensing, registration or qualification, usually of a less burdensome nature than full qualification, which in some cases is not available at all to savings banks. A word of caution with respect to such legislation which defines permitted activities. Such activities should be carefully scrutinized to

make sure they cover all the acts necessary to preserve the bank's interest, including servicing and buying in the property on foreclosure and holding the same for a reasonable period. In this connection it is well to remember that the Administrator of Veterans Affairs has the option to refuse to set an upset price, in which event the holder will have no right to transfer the property to the VA.

Taking a long range view, the investor must always consider that the trend of legislation in periods of depression and foreclosures may take an opposite direction. Qualification may later be necessary, either because of new court decisions or because of foreclosure and the ownership and operation of properties thereafter. For that reason, where qualification is readily available without excessive cost and without undue exposure to local taxation, we have advised our clients to obtain and maintain such qualification. In most such states, qualification in and of itself has not resulted in subjecting a qualifying

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bank to local taxes in a substantial amount.

About a year ago I made a rough classification of the states where we have considered this question. (See "Out-of-State Mortgage Investments," published by ABA, March, 1954.) Since that time there have been several favorable developments through state legislation. There are now four main classifications with regard to this question:

In the first group are such states as Alabama, Arkansas, Florida, Illinois, Kansas, Michigan, Missouri, Nevada, North Carolina, Oklahoma, Oregon, Tennessee and Texas, where express statutory authority and administrative policy give assurance that the purchase (and in some cases the making) of mortgages on properties located there, as well as the servicing and enforcing of such mortgages are activities which do not constitute the unlawful doing of business and which do not give rise to local taxation of the lender by the state.

A second category, including California, Colorado, Pennsylvania, Virginia, Washington and Wisconsin, is one where the carrying on of a mortgage investment program, without qualification, might well constitute the doing of business and would be sufficient to preclude resort to local courts by an unqualified foreign corporate investor. In these states the defect may be cured, since the bank may subsequently qualify and thus remove its disability to sue on the mortgage contract. However, a monetary penalty, often severe, may also be incurred.

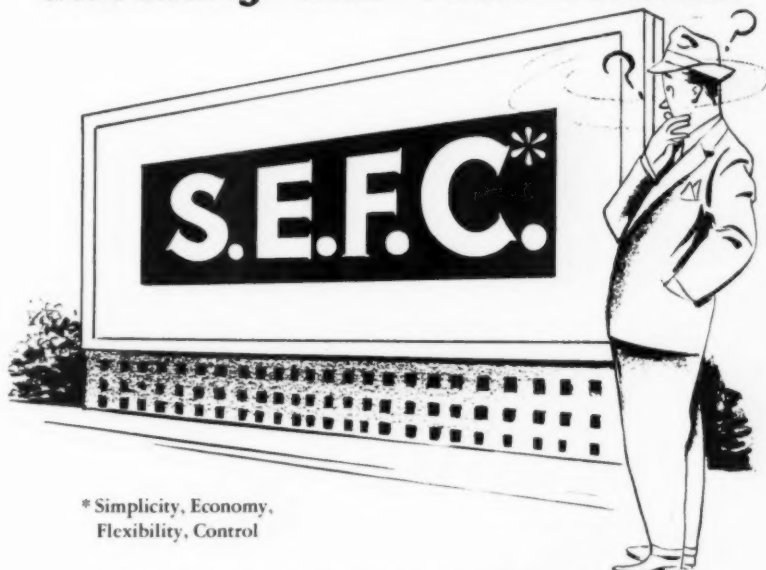
Third, there is a more troublesome group which includes Arkansas, Idaho and Utah. In these states, the contracts of an unqualified corporation made as a result of unlawfully doing business in the particular states are void and unenforceable by it and its assigns. [See *John Hancock Mutual Life Insurance Company v. Girard*, 64 Pac. 2d 254 (Idaho, 1936).] This results in a disability to sue which cannot be cured by subsequent qualification. Obviously, in such states investment is out of the question unless the bank first qualifies or can obtain an unconditional legal opinion that its purchase, servicing and enforcement of loans are not tantamount to doing business. It is evident that in

these states a seller's failure to qualify while doing business in the state may invalidate a mortgage even after it is acquired by the bank. Thus it is essential for a bank not only to avoid the unlawful transaction of business in these particular states, but also to make certain that previous holders of the mortgage investments have done so.

The fourth classification includes

those states, too numerous to specify, in which special considerations apply with respect to qualification or limiting activities. Drastic money penalties for a failure to qualify may be imposed on the corporation, as in Indiana, or on its officers, as in Maryland. Certain necessary activities in connection with mortgage investments such as servicing may be held to constitute doing business in states where banks

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cannot qualify, as in Connecticut. In other states where banks cannot qualify, it may be determined that permitted activities not constituting doing business are sufficient to carry on a mortgage investment program, as in New Jersey. Tax consequences of qualification plus penalties for failure to do so may make certain areas, such as the District of Columbia and Hawaii unfavorable for mortgage investment.

There is a legal theory which is reflected in many state court decisions that isolated transactions by unqualified corporations, even though they are of a nature which would constitute doing business if regularly repeated, will not of themselves constitute doing business. We have felt it prudent not to rely on this rule because of its indefiniteness. For example, it is possible that even a single purchase of a large block of mortgages might be held not to constitute an isolated transaction.

Local taxation is not so readily classified. Few states are wholly free from some tax worry, though many are no problem so long as no mortgages are foreclosed. Perhaps Florida wins the medal for no taxation, with no income or franchise tax and banks exempt from capital stock tax. Aside from money paid out, some state tax returns are troublesome to complete and file annually, such as Alabama, Louisiana, Ohio, South Carolina, Utah and Virginia. There are numerous states requiring small annual filing fees of \$25 or less. Where there are income or franchise tax returns the usual experience is that foreign banks observing the precautions are not taxable on the basis of income from mortgage investments in the state concerned, and pay only a nominal minimum tax, if any. Among the states where the restrictions on activity must be most rigidly observed are Georgia and Virginia. Once properties are foreclosed and bought in by a foreign bank, property ad valorem tax liability would arise, and the property tax burden would be more severe in a number of states which levy annual property taxes. These include Arizona, California, Georgia, Indiana, Kentucky, Maryland, Rhode Island, South Carolina, Utah, Virginia and Wisconsin. Should foreclosed properties be operated by the

bank the income from such operation would possibly be taxable under local income tax laws, but in no case have we been advised that such taxation would "contaminate" the unforsclosed investments to render them also taxable.

Even though a bank may have qualified in a particular state, we believe it is important carefully to limit its lending practices in that state. By so doing the bank will reduce to a minimum its exposure to local taxes which, of course, could seriously affect net yield. We have recommended to our clients that, regardless of qualification and subject to local variations, they strictly limit their lending activities in states other than the one of their origin as follows:

» Limit site inspection of properties and subsequent inspections to the absolute minimum.

» Maintain no offices or employees in any states except a statutory representative where required.

» Refrain from instituting or carrying on any negotiations in the state

and make certain in each instance that all negotiations are consummated in the state of the client's origin.

» Commitments and contracts for the purchase of mortgages should by their terms be contracts governed by the laws of the state of the client's origin and should be executed by the client only in such state.

» Commitments should be issued directly to the seller of the mortgages and not to brokers.

» To the greatest extent possible, avoid or minimize all relationships with servicers, brokers, mortgage companies, originators and the like which might give rise to the existence of an agency relationship in the state.

» Be certain, before issuing a commitment to purchase loans, that the seller is obligated to make the loans regardless of the issuance of the commitment.

» Close all purchases of mortgages, and disburse all funds, either loan proceeds or purchase price of mortgages, in the state of client's origin.

» Make serious efforts to dispose of

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foreclosed property as promptly as possible and avoid operation of such properties to the greatest extent possible.

» To as great an extent as possible use servicing contracts under which the servicer is an independent contractor, rather than the agent of the investor.

The third legal problem—FHA and VA regulations—is not peculiar to out-of-state lending, but it may be new to banks formerly concentrating on conventional lending within their own states and unfamiliar with governmental insured or guaranteed loans in the wider market. For example, how far may a bank rely on the FHA or VA evidence of insurance or guaranty? The National Housing Act and the Servicemen's Readjustment Act of 1944, as amended, both contain so-called "incontestability" provisions designed to protect the purchaser of a guaranteed or insured loan against invalidity of the governmental insurance or guaranty which might result from failure of the originator or previous holder to comply with the governmental regulations. Unfortunately, this protection is not free from doubt, particularly in the case of VA mortgages, where the protection is given to a holder "without notice." What is absence of notice? If the new holder should have known from the loan documents or from other sources that the purchase price exceeded the reasonable value fixed by the VA, can it claim immunity from its imprudence? What loan documents is it imprudent not to require to be submitted with the loan papers? It is made more difficult to ignore or not require VA papers such as the certificate of reasonable value, the VA commitment and the certification of loan disbursement because of the widespread practice of prudent lenders of requiring and inspecting these papers.

There is another aspect of this problem where the bank has any sort of continuing relationship with mortgage originators. To what extent may the government claim that an agency relationship exists between bank and originator, thus imputing a breach of regulations by the latter to the former? The opinion of the VA solicitor (now general counsel) of December 12, 1950 is to the effect that an agency relationship does exist.

For these reasons, many institutional investors have taken the conservative view, with which I concur, that all pertinent VA and FHA papers be examined along with the examination of the legal papers, for conformity with applicable regulations. We do this having in mind a possible time (which I hope never comes) when there are widespread foreclosures and claims on governmental insurance contracts and guaranties. It is not inconceivable that in such case these agencies will take a close look at the claimant's contract rights.

And here is a practical matter which concerns many out-of-state lenders: how to assure speedy payment to the out-of-state originator. This is of interest to the bank as well as the originator, since it helps the originator to furnish future loans using funds otherwise tied up. One method, used with originators of good credit and stability, is to purchase immediately upon shipment of the papers, subject to repurchase by the originator if the bank's legal examina-

tion discloses defects. A second method, widely used in recent times, is the employment of a commercial bank as a source of interim financing, such bank accepting a pledge of the papers or purchasing the loans subject to repurchase. This latter method of interim financing, recently under a cloud but now apparently approved by such credit authorities as Federal Reserve Bank, has the great advantage of permitting the savings bank to time its acquisition of loans to the availability of funds, while assuring prompt payment to the originator.

Any bank entering upon an out-of-state mortgage program would do well to instruct its originators carefully in advance as to its legal requirements for acceptable mortgage investments. This simple step will repay many times over the effort in avoiding time consuming and sometimes costly delays in obtaining corrections and additional documents where distance and differing legal practices make errors doubly irritating and burdensome.

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POPULATION GROWTH

(Continued from page 23)

They will become slightly more numerous during the next several years. After 1960, the college age population will grow rapidly, as the large number of persons born during the war and postwar years reach 18 years of age.

These statistics on school age children illustrate one important way in which population developments affect the demand for government services. The specific impact in terms of building new school facilities and recruiting teachers is a problem many communities are continuing to wrestle.

The Gain in Households

When, as for housing and certain types of home furnishings, the household is the basic unit of demand, it is the relevant factor for analysis. A household is a dwelling unit occupied by one or more persons; it is distinguished from a family which is defined as two or more persons related by blood, marriage, or adoption and living together. The difference between the number of households and primary families (those including the head of a household) are primary individuals, who are defined as household heads living alone or with non-relatives only.

Married couple families comprise over three fourths of all households. Other primary families are about 11 per cent of the total and primary individuals account for the remaining 13 per cent.

The number of households in the United States was estimated at about 47.8 million in April of last year. This represented an average annual increase of about 850,000 since March 1950. The annual increment since 1950 has been lower than during the latter part of the 1940's but higher than during the early 1940's. In the late 1940's, the annual increase numbered about 1.5 million and from April 1940 to April 1947, about 600,000.

The same basic factors influencing family formation, as well as some additional ones, affect the number of households. In our society, most married couples desire to maintain separate living quarters when economic

conditions permit it. Although the marriage rate was high during the early 1940's and the war years, the impact on household formation was offset by continued doubling of families and subfamilies. During the latter part of the 1940's, the marriage rate continued high, and with high income the amount of doubling declined. As a result, the average number of husband-wife households increased almost 1.2 million a year from 1947 to 1950. With the number of marriages dropping off, the average annual increment of married couple households was only about 400,000 during the first half of the 1950's. Undoubling of families continued but the magnitude was smaller than during the late 1940's.

In connection with number of households, it is of interest to note the influence of the changing age composition of the population. More aged couples are now maintaining their own households, partly because of their favorable income positions and partly because they are more numerous.

The influence of changes in marital status also is reflected in household formations. Widowed and divorced persons form an increasing proportion of our population. During the recent years of high income, a growing proportion of them, as well as of single persons, have separate living quarters. About a third of the annual increase in households during the first half of the 1950's was due to the larger number of individuals maintaining their own households.

Assuming continued favorable economic conditions, it is possible that an even larger proportion of individuals will maintain their own households. This would bolster the rather meager number of households to come from marriages during the next five years. Nevertheless, household formation during this decade will be low compared with years immediately preceding it and with the years after 1960 when the wartime babies reach marriageable age.

A Mobile Population

A moving population also leaves its mark on demand. During the war and postwar years, a substantial part of the population has been on the go. Nearly a fifth have changed their ad-

dress each year since 1947. The number moving short distances (within the same county) is by far the larger proportion of movers. Much of this movement represents the shift of population from the city to the suburbs.

About 3 per cent of the population has migrated into a different state each year during the last 7 years. In large measure, this movement is associated with the very high rate of population growth in the far west.

Probably the major effect of these population shifts is a redirection of demand, although it has quantitative effects as well. For example, the demand for community facilities has been higher by reason of migration. The number of housing starts also probably has been affected by the suburban movement. In this case, however, the major impact has been on the kind of housing constructed. Single-family dwellings have become a larger proportion of new residential building. This development in itself has had far-reaching implications. From it have sprung a host of requirements for items such as plants and shrubs, lawn seed, yard equipment, and house maintenance materials and tools.

Trek to the City

While considering the demand for housing, an aspect which cannot be neglected is the migration of population from farms to cities. Recent Census data indicate that the number of farm households declined about 150,000 a year during the first half of the current decade. This shift has had an important impact on the demand for nonfarm housing.

The purpose of this article has been to describe some recent developments in the Nation's population and to suggest some of the implications for demand over the long term. It has been necessary, of course, to recognize—explicitly in several instances—that other factors also govern the long-run volume and composition of demand. As a matter of fact, a multitude of interacting forces—including population factors, income, standards of living, and technological change—come into play on demand in the long run. For purposes of analysis, however, it is logical and desirable to consider the factors separately.

President's Page

SINCE all of us know that 1956 will be a "political" year it seemed to me that almost the first thing I ought to do as MBA President was to arrange to meet some of the members of Congress, and the housing and credit policy making officials in Washington, and to talk with them about our business.



Lindell Peterson

My three-day visit coincided with a special round-table on the mortgage credit situation conducted by Senator John Sparkman (D. Ala.), the Chairman of the Subcommittee on Housing of the Senate Banking and Currency Committee. Among those participating in this discussion were MBA's former president, William A. Clarke, Robert M. Morgan, of the Boston Five Cents Savings Bank, and R. Manning Brown Jr. of the New York Life, all of whom helped effectively to describe, for the benefit of the Subcommittee, the operation of the mortgage market, with particular reference to current conditions.

HHFA Administrator Cole and the other housing agency heads made clear that the specific problems of the mortgage market would not be overlooked in the formulation and carrying out of general credit policy. William McC. Martin, Chairman of the Board of Governors of the Federal Reserve System, presented an extremely lucid statement about the influence of monetary policy on the mortgage market. Mr. Martin's statement is printed in this issue.

At the conclusion of the hearings, our General Counsel arranged a luncheon which was attended by MBA board members in the vicinity of Washington and more than twenty of the leading federal officials who, in one way or another, influence the course of our business. Among those present were Mr. Martin, Dr. Randolph Burgess, the Under Secretary of the Treasury, Commerce Under Secretary W. Walter Williams, Dr. Arthur F. Burns, Chairman of the Council of Economic Advisers, and Council Member R. J. Saulnier. The HHFA Administrator was away on a speaking engagement, but his new Deputy Administrator, Frank Meistrell, FHA Commissioner Norman Mason, Ralph H. Stone and Thomas J. Sweeney of the Veterans Ad-

ministration, FNMA President J. Stanley Baughman, and Chairman Walter McAllister and the members of the Federal Home Loan Bank Board, were all with us.

Later I discussed at some length with Mr. Meistrell the difficulties being encountered in the urban renewal program and talked with Mr. Mason about FHA matters. As he stated in his speech at the Los Angeles convention, Mr. Mason is concerned that some mortgage lenders may not be adhering strictly to FHA principles in the conduct of their closing and servicing activities. The same subject was covered in a conversation with VA's Tom Sweeney. Although I am without any direct knowledge of the matters referred to, I very strongly recommend to the senior executives of our member organizations that they, personally, thoroughly review their operations to assure that no irregularities have crept in. MBA's Counsel is preparing an article on this subject for publication either as a Letter to Members or in the next issue of *The Mortgage Banker*.

Altogether, I felt that my visit was successful in renewing and broadening the contacts between Washington officialdom and our Association. There is every evidence that these contacts will be important to us in the crucial months ahead. In order to be better prepared for what looks like a rugged legislative year, Vice President Austin and I are meeting with the full Legislative Committee in Washington on January 22 and 23, with a view to having policy recommendations ready for presentation to the Board of Governors at its February meeting.

Among the subjects with which we shall be concerned are: insurance of mortgages on medical facilities; special mortgage insurance for elderly people; flood damage insurance; public housing; urban renewal; cabinet status for HHFA; extension of the VA loan guaranty program, and the possibility of public criticism of the industry in months ahead in connection with discounts on FHA and VA loans.

A stylized cursive signature of Lindell Peterson.

PRESIDENT

INTERIM FINANCING

. . the experience of MBA members

Part II of Research Committee's Interim Financing Report Financing Construction Loans to Builders

Compiled and analyzed by L. J. Holt, Philadelphia, Chairman of the Research Sub-Committee consisting of Charles J. Horn, Newark, Irvin Jacobs, Chicago, and John F. Schneider, New York; Robert H. Pease, Chairman, MBA Research Committee; and L. O. Kerwood, MBA Director of Education and Research.

MORTGAGE bankers throughout the country were asked in a survey by the Research Committee to give their methods and procedures for operating their construction loan departments. This article presents many of the important features of that survey. With construction loans an important source of revenue for the mortgage banker as well as a valuable service to the builder, it is hoped that these suggestions will make construction lending easier, safer and more profitable. It is essential to remember that these practices will vary somewhat in different states and in different areas, but the *basic principles* will have wide application.

One of the major problems is the inherent doubt, by many commercial banks, of the soundness of financing builders during construction. This places the burden on the mortgage banker to convince his own banker that the methods used, and safeguards provided, by the mortgage banker are sufficiently adequate to remove most of the risk from construction financing. The following methods for accomplishing this have been successfully used by MBA members:

» Require signed financial statements, both of the builder's company and of the builder personally, from every builder at least once a year.

» Have construction loans signed personally by the builder. In some cases, the builder signed personally for a part of the loan rather than for the entire amount. This accomplished two things: it added further financial

strength to the note and, of equal importance, it made certain that the builder would complete the buildings to the limit of his resources. When the builder is personally responsible for the debt, he will use every means at his disposal to finish the job as quickly and as efficiently as is possible.

» Upgrade your builders by financing only those who have demonstrated their ability to operate profitably and who have built houses that sell quickly. Their financial statements for several years will show whether they have and can build at a reasonable profit. The sales record of several of their jobs or projects will indicate how their houses have been accepted by the public. A slow construction job is costly for the builder and for the mortgage banker. A project that fails to sell quickly is a serious drain on the builder and results in difficult delivery problems, for the mortgage banker, with his insurance company. These difficulties can be prevented by financing only successful builders.

» Keep a close relationship between sales of houses and construction loans. Some MBA members limit their builders to 10, 25 or 50 construction loans ahead of actual sales. This varied, of course, with the financial abilities of the builders. The important feature with this control is that neither the builder nor the mortgage banker is seriously involved in the event of a set-back in the sales market. If the builder put in several hundred basements and the mortgage banker commits for the entire

group of construction loans only to find that the sales market will not take the houses, then both the builder and the mortgage banker are in serious trouble. Such problems are of concern to the mortgage company's bank and the above procedure is one way of solving it.

» One of the real safeguards in making construction loans is a good building inspector in the employ of the mortgage banker. MBA members who make a substantial volume of construction loans are almost unanimous in their opinion that good building inspections by the mortgage banker are an absolute necessity. These inspections check both the quality and the quantity of the building operations. Since all construction advances are made on the basis of how well the work is done and how much has been completed, the role of the inspector is very important. MBA members reporting for the Research Committee's survey did not pay out only on the FHA or VA inspection reports, the majority had their own building inspectors.

» The two big risks in construction lending are those of being unable to finish a building project or being unable to sell it upon completion. Many MBA members keep a constant check on the sales market in their area, and go to considerable lengths to keep this market survey accurate and up-to-date. This report is checked at least every month for all price classes of homes. A mortgage banker who has an up-to-date understanding of the

sales market and who bases his construction financing on a conservative estimate of the sales market is a source of great comfort to the commercial banker and will obtain larger lines of credit from the bank for construction purposes.

» Many MBA members have difficulty with past-due construction loans to their bank. This is caused by improper dating for the maturity of these loans, by slowness of builders in construction work, by delays at the FHA and VA and by shortage of certain materials. Most of these problems can be corrected and respondents in the survey submitted many valuable suggestions for so doing:

1. Many members make their loan papers with a date based on the actual time of the first payout.

2. The mortgage banker's inspector can accelerate a slow building operation—the builder is made aware that his slowness can jeopardize future credit extension.

3. When real material shortages exist, the builder is advised to purchase advance requirements and to store in a warehouse. Some MBA members help the builder finance the purchase of such material.

4. Construction loans are not opened unless the material is available in the warehouse of the builder.

» Good waivers of lien and accurate construction statements for every trade are mandatory for a properly-run construction loan department. Many MBA members have their own lawyers check their waivers of lien and the more efficient departments have very meticulous procedures for seeing that every waiver is absolutely correct. It was the unanimous opinion of the firms reporting, that extreme care must be used in checking each waiver of lien. The great majority of MBA members stressed the importance of seeing that the houses could be built for the amounts indicated on the construction statement.

If the above safeguards are carefully and totally maintained, and if the mortgage company's bank is fully aware of the degree of protection furnished by the mortgage banker in the handling of construction loans, then the bank is not only willing but is glad to provide the mortgage banker with funds for making a substantial volume of construction loans. Replies to

the survey indicated that the amount of funds made available for construction loans by a bank to a mortgage banker is more proportional to the confidence of the bank in the *manner* in which the mortgage banker handles his construction lending, than is the amount proportional to the *capital* of the mortgage banker.

Many MBA members reported that obtaining firm commitments from a life insurance company for the purchase of the loans when sold to a satisfactory buyer was a requirement of their commercial bank. In this period of quotas for FHA and VA loans, and of uncertain price quotations for mortgages, the need for firm commitments for the final loans should also be a requirement by the mortgage banker. This is particularly true of project cases. MBA members point out that between six and nine months will elapse between the time the construction loan is negotiated and the loans are ready for delivery; therefore, the mortgage market is too uncertain to make a deal that does not have a forward commitment. If the builder is strong enough financially to protect the mortgage banker with a substantial guarantee on the price of the loan then some risk may be warranted, but the mortgage banker must be aware that there have been several times in the past few years when his principals did not have funds for FHA or VA loans. A firm commitment is the safer method.

Practically all MBA members require completion bonds for larger commercial buildings and also for sewer, water and street construction on housing project loans. The exact nature of these completion bonds should also be carefully examined, for the mortgage banker must have these services completed before he can have his loans insured. In the case of commercial construction loans, many of our members require that a certain per cent of the space be already leased and that a firm commitment for the purchase of the final loan be obtained before the construction loan is opened.

Many MBA members report that the rate of interest paid to their bank is the same rate as charged the builder, with their profit coming from the *fee* paid by the builder. Many other MBA members borrow from their banks at a lower interest rate

than they charge their builder, and they also receive a fee from the builder. Local conditions will cause this practice to vary, but it is logical that if the mortgage banker furnishes all of the services and safeguards listed earlier in this report, he must have a higher rate from the builder in order to operate on a profitable basis. The bank is depending on the credit of the mortgage banker and upon his proper handling of payouts for protection to the bank; if these are furnished by the mortgage banker, then he is entitled to a higher interest rate from the builder. This rate differential seems to vary between $\frac{1}{2}$ and $\frac{3}{4}$ per cent. The rates and fees must of course, be in accord with FHA and VA regulations, but a reasonable increase over the bank rate is certainly warranted.

The per cent of the construction loans to the cost, value, or sales price of the house showed a wide range, varying from 50 per cent to 75 per cent with no uniformity being evident. The number of payouts during construction varied from two payouts every week to a total of four payouts as work progressed. One common answer was evident—the loan account should *always* contain sufficient funds to complete the building. Some firms paid the sub-contractors, while others paid the builder and he dispersed to his sub-contractors. This matter varied with the responsibility of the builder.

Many members operate by obtaining an FHA dual commitment and a commitment from their insurance company to purchase either in the builder's name or to a qualified FHA purchaser. One area of the country is now operating on the basis of a title company furnishing a guarantee of the waiver of lien. This is an ideal arrangement for both the mortgage banker and for his bank. While this method was reported in use in only one large city, it is a most interesting innovation.

Of particular importance is the trend of obtaining funds from widely separated parts of the country by mortgage bankers. Many large banks provide MBA members with funds for construction loans at distances of a thousand to two thousand miles. This flow of money from financial centers
(Continued on page 51)



Voice of the Home Office

What Happens When "Rate Is Broken"

These observations by a life company official were not intended to represent an investor-correspondent problem but are some thoughts about conventional lending—and, in addition, he has something to say about rate cuts.

IN conventional loans, as contrasted to insured and guaranteed loans, each case is a separate and distinct entity and requires thought and judgment in arriving at a recommendation. Too many persons now in the mortgage business have been working with insured and guaranteed loans for so long that they are rusty or have never developed the faculty of arriving at a sound appraisal and then properly underwriting the applicant's credit. There is a tendency to take current sales price as value and, so long as monthly income is four and a half or five times housing expense, everything is considered to be all right. We all know that it cannot be as simple as that.

We need scrupulous integrity and investigation of all facts pertinent to the purchase and loan transaction. Conventional loans are normally consummated with the investor having complete reliance on the conditions and statements recited by the correspondent and are truly a mutual trust business. A loan is not necessarily unattractive to a lender if all factors are not 100 per cent. The lender would much rather have a concise and factual statement by the correspondent of any unfavorable factors—such a statement will prejudice him less than something he might find which would indicate the possibility of unfavorable factors being present but not mentioned or commented on in the correspondent's report.

We have noticed a lamentable ten-

dency on the part of aggressive correspondents to get their principal to agree to a preferential interest rate or other gimmick in order to secure a temporary competitive advantage. Obviously, correspondents for life companies are rarely, if ever, the sole source of conventional loans in any city. In many areas, however, they are a substantial and important factor. Consequently, if a drop in interest rates shows up in their community, which proves, after investigation, to be merely for temporary competitive advantage, it would be wise for the

correspondent to report the condition to their principal and to fill up the low rate lender as promptly as possible while holding fast to the warranted higher interest rate.

Too often in the past a break in rate has quickly been followed by a large majority of the lenders and, when the dust settles down, everybody is doing about the same percentage of business and the investor is getting $\frac{1}{4}$ or $\frac{1}{2}$ of 1 per cent lower return. Rarely has a drop in interest rates been caused by pressure from applicants and borrowers. Almost always it has been due to the cupidity of some lender in the area.

The Chicago MBA has published its first "Markets for Various Types of First Mortgage Real Estate Loans"—the first such undertaking of any local mortgage group. Every member firm is shown with the types of loans in which each one is interested.

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Voice of the Correspondent

Most Vulnerable Point in Mortgages

Delay in getting applications approved, inconstancy of his source of funds, failure of investors to keep in touch with local conditions—these and other factors make the correspondent the most vulnerable point in the mortgage industry, says this correspondent.

THE position of the local mortgage correspondent in the mortgage industry today probably is the most vulnerable point in the entire industry. Vulnerable because:

» The correspondent must compete with local lending institutions using tools which, all too often, he has had little voice in fashioning. The tools, in the way of loan-to-value ratios, appraisal procedures and techniques, prepayment options, interest rates and amortization patterns are often set by finance committees who are far removed from the hue and cry of the day-to-day struggle in the local market place for prime mortgage loans.

» He is a party to an agreement which in theory is bilateral. This agreement is based upon mutual trust and understanding. By the nature of the subject, great reliance must be placed upon the correspondent's integrity, ability and his long-term views for the future of his business as a continuing operation. Yet, all too often in actual practice, excellent loans are lost because they do not conform precisely to a cut and dried pattern set by the home office finance committee; and, instead of relying upon the same trust, understanding, ability and knowledge which underlies the relationship, the correspondent's recommendation is ignored and the "pattern" invoked. Thus, another excellent loan is added to the portfolio of a local institution whose "pattern" is flexible enough to permit it to recognize merit in a loan even though it does not meet every requirement of their "pattern."

The above generalities resolve themselves into specific conditions which hurt the correspondent in his competitive position among the local institutions in his area. Some of these specifics are:

» *Delay in approval of applications.* Many local institutions offer a decision on a loan application in twenty-four to forty-eight hours, whereas some correspondents frequently have to wait a week or longer for home office decisions.

» *Inconstancy of his source of funds.* Many correspondents find themselves "out of the market" with very little warning from their principals, and consequently, lose valuable clients to local institutions who can offer a constant source of mortgage funds. Needless to say, it is most difficult to woo these clients back into the fold when the correspondent can joyfully announce that he is "back in the market." Many of these clients will not return, because they have discovered that the local institutions can offer terms and rates as attractive as those offered by the correspondent. In the past few years, savings and loan associations have reduced their rates and terms to the point where they are closely comparable to those offered by life companies. Thus, the correspondent is fast losing one of his most potent competitive tools.

» *Failure to keep in touch with trends in the local area.* This would seem to be the fault of the correspondent for not keeping the home office informed, but in many cases it is not. Excellent lending areas are excluded because no one on the finance

committee has seen the area for many years and cannot visualize the tremendous growth and change that is taking place in many cities.

On the constructive side, many home offices have found the methods to improve these conditions. The following suggestions are practical, because they have worked in practice, and offer solutions to many of the difficulties mentioned.

1A. An arrangement whereby small committees of two or three members of the investment department can review and approve loans daily, up to a specified amount. Many correspondents are getting twenty-four to forty-eight hour replies by this means.

1B. Permitting the correspondent to approve certain types of loans immediately up to 10 per cent or 15 per cent of his portfolio of conventional loans, without the necessity for further approval by the home office.

2. A guaranteed minimum quota made known to the correspondent well in advance of the time the funds are to be used. By proper budgeting and a knowledge of *minimum* funds available for mortgages, this can be done.

3. Frequent field inspection trips by policy level members of the investment department or finance committee. This is such an absolute necessity that it is ridiculous to set it forth, because without an on-the-spot knowledge, the value of the correspondent's recommendations cannot be properly weighed. Trends and growth in the local area should be observed and understood in order to do a proper job of lending in any area.

The writer has seen the results that can be obtained by the means outlined above—and they are good. Not only will the principal obtain a better portfolio, but the correspondent will be on more even footing with the local institutions with whom he is competing.

New MBA Senior Conference for SMU

The principal expansion in MBA's educational program in 1956 will be the addition of a second annual Senior Executives Conference to be held late in March in Dallas, in cooperation with the school of business administration of Southern Methodist University. Inauguration of this second Conference comes after a decade of similar meetings at New York University.

The Senior Executives Conference is something entirely unique, not only in the field of education, but in trade association activities as well. At NYU, as it will be at SMU, attendance will be limited, not more than 120, to preserve the academic atmosphere under which member firm representatives will gather to study, under guidance of competent scholars, the broad general trends and influences in the industry which vitally affect day-to-day business decisions.

Dean Laurence Hobart Fleck of the

SMU school of business administration, will direct, and assisting in the initial organization of the course is the Southwest's leading economist, Dr. Arthur Smith of the First National Bank in Dallas and Jerry B. Frey, Jr., Brown-Frey Mortgage Company, Dallas.

Arrangements at SMU provide for those attending to stay at Dallas' new Statler Hotel, with the sessions in SMU's new school of business building. The overall direction at SMU, as at NYU, will be under L. O. Kerwood, MBA director of education and research.

The new SMU Senior Executives Conference is designed primarily to make available this type of educational opportunity for more MBA member firms. While its geographical location indicates that it is being established to serve the western part of the country, it is likely that members from all sections will attend just as they do at NYU.

NYU Senior Course January 24-26

While the SMU Conference is an event for later in the winter, the 11th annual Senior Executives Conference at NYU January 24-26 is at hand. Those who have not yet made application to attend should act promptly. Registration limitations apply, and members are cautioned to submit only one application from a firm, taking care that the applicant is at the management and policy-making level, the group for whom the Conference is designed. The program is built on the theme of Mortgage Lending in a Period of Rationed Credit and the program itself is deemed one the best and most timely that has been offered. It includes:

Elements of Strength in The American Economy by Dr. Marcus Nadler, NYU professor of finance and research director, Institute of International Finance.

Elements of Weakness in The American Economy by Dr. G. Rowland Collins, dean of the NYU graduate school.

Second session theme is The Shortage of Mortgage Money and the speakers are:

The Supply of Savings for Mortgage Investment by Dr. Roger F. Murray, vice president, Bankers Trust Company, New York, and



Carey Winston



L. O. Kerwood

Analysis of the Demand for Mortgage Funds by Dr. George Cline Smith, economist, F. W. Dodge Corporation.

Third session topic is The Future Market for Homes and the speaker is Dr. Gordon W. McKinley, director of economic research, The Prudential

Insurance Company of America.

At the fourth session the topic is Government Controls and Mortgage Credit. The speakers are:

Federal Reserve Policy and Mortgage Credit by Dr. Roy L. Reiersen, vice president, Bankers Trust Company, New York, and

The Home Loan Bank Board and Mortgage Credit by W. W. McAllister, chairman, Federal Home Loan Bank Board.

Fifth session topic is The Diversion of Savings from the Mortgage Market. Speakers are:

The Stock Market and Future Mortgage Demand by Dr. Jules I. Bogen, NYU professor of finance,

Consumer Spending and the Trend of Savings by Martin Gainsbrugh, chief economist, The National Industrial Conference Board, professor of economics, New York University.

MBA in Education

Not every MBA member appreciates the fact that the Association's program in education is one of the most comprehensive ever undertaken by a national trade group—or that it represents one of the most valuable contributions by any group to the industry it serves. Less than a decade ago, all the Association's activities were less than the educational program alone now embraces. Every year without exception something new has been added, improvements made in some one or more departments. This year will be particularly important in that respect. On these pages are reports of some current developments in MBA in Education, with the principal effort, the School of Mortgage Banking, to be reported later.

Carey Winston, Washington, D. C., is chairman of the MBA Educational Committee, Addison K. Barry, Newark, is chairman of the MBA-NYU subcommittee directing the Conference with the overall direction by L. O. Kerwood, MBA director of education and research. Dr. H. W. McDowell of the NYU graduate school will direct for NYU.

Alumni for the MBA School Planned

Something new has been added to the MBA educational program with the organization of the Alumni of the School of Mortgage Banking, under which any student from a member firm who has been awarded a Certificate of Merit in the program, or who has completed the curriculum of the School and has been graduated, will be eligible for membership. The objective is to perpetuate an enduring interest in the Association's School of Mortgage Banking.

The idea for such an organization was put forth and initially developed during the school session in the summer of 1955. Since that time, the Committee, consisting of Chairman George W. Lubke, Jr., George W. Lubke, Inc., Daytona Beach; Carl Sandquist, Coast Mortgage & Investment Company, Seattle; Robert O.

Heim, The Brooklyn Savings Bank, Brooklyn; Malcolm A. Belt, American Security and Trust Company, Washington, D. C.; Charles H. Kopke, Commerce Trust Company, Kansas City, Mo.; and Richard J. Donovan, Bank of America, Pleasant Hill, California, has worked to effect an early-functioning organization.

After this initial work, the organizational committee proposed to the MBA Board the organization of the Alumni and it has been approved. In addition to the group's educational activities the alumni will hold a regular meeting each year at the annual Convention.

This year will see the graduation of the first class from the School of Mortgage Banking, with the ceremony to be held at the 1956 annual Convention in Chicago.

MBA Home Study Course Develops

Another valuable feature of the MBA educational program with which most MBA members never come in contact is the comprehensive home study program, which is a part of the School of Mortgage Banking curriculum.

Since June of last year home study program II(a) has been added, dealing with the economic factors affecting the industry and the work and influence of the Federal Reserve System.

To be developed for the first time will be Home-Study Program II(b), dealing with the analysis and interpretation of financial statements of the industry.

Both Home-Study Program I(a), concerned with financial institutions of the country, and Home-Study Program I(b), based on the MBA textbook, *Mortgage Banking*, have been revised in the light of the past year's experience in using the materials.

Dr. Homer V. Cherrington and Dr. Harold W. Torgerson, both of Northwestern University, have made important contributions in the development of this phase of The School of Mortgage Banking.

Course II at Stanford

The MBA Educational Committee has announced that Course II of the School of Mortgage Banking will be introduced at Stanford University this summer. This part of the curriculum of the School has to do with the financing of income properties, and has already been introduced at the Northwestern University School.

Dates for Course I, to be repeated again this year at Stanford, are July 29-August 4 and dates for Course II are August 5-11, 1956.

Still another addition to the curriculum of the School of Mortgage Banking will be the introduction, in 1956, of Course III at Northwestern University. This phase of the curriculum will deal specifically with mortgage loan investment policies and practices. Dates for Courses I and II at Northwestern University will be June 24-30, and dates for Course III will be July 1-7, 1956.

Hold 1956 Meeting for Business Deans

Of all the many MBA activities in recent years, both in educational work and in the general program on behalf of the mortgage industry, probably none is basically more important, or holds greater prospect for advantages for mortgage banking, than the Association's Conference on Mortgage Banking for Business School Deans and selected faculty members from colleges and universities. It was held last June at the University of Michigan under the auspices of the institution's school of business administration, with more than thirty-six educators attending. It was not strictly an Association activity, but was sponsored by the Research and Educational Trust Fund of the Mortgage Bankers Association of America, the first broad activity undertaken by this charitable trust. The objective was to get together a representative group of midwestern educators from principal universities and colleges to study, in a brief period, all activities and procedures which make up the modern mortgage industry. No industry has expanded more rapidly and has

changed more in the past quarter century than the mortgage industry. These changes have created new responsibilities and new requirements—and one of them is certainly the increasing need for more and better trained personnel.

Thus, one motivating factor behind the educators conference at Michigan was to go to one of the fountainheads of learning that is, to the educators in the schools themselves, tell them what this new, modernized industry is, how it operates, the influences which affect it, all with the hope that they will be in a better position to guide coming generations in their choice of careers and, of course, always with the hope that more and more will turn to the mortgage field.

There is to be another educators' conference in 1956—date, place and sponsorship to be announced. Again there will be a complete switch from the normal—the students are the business school deans and faculty members, while the faculty will be MBA members from leading mortgage lending and investing institutions.

EDUCATION

Trust Fund Plans and Objectives

In MBA's educational activities, one of the major efforts—it may develop into the major effort—is yet to come. It is the work which the Research and Educational Trust Fund of the Mortgage Bankers Association of America will do when it has completed its plans and made all arrangement to do the comprehensive job for the mortgage industry which it contemplates. The University of Michigan Conference for Business School Deans and affiliated faculty members has been its major undertaking so far; and the success of this initial excursion into the field of education and public relations has done nothing so much as point up and emphasize the need for more effort along these lines. In an article on the preceding page is told the plans for another Conference in 1956—time and place to be announced soon.

The Trust Fund will do a great deal more in the field of education

than this selective instruction of educators in college and universities. It will explore every educational field to determine where the Association can make a contribution for more and better education about mortgage banking; it expects to make it possible for more and more young people to have the opportunity to select mortgage banking as a lifetime career; and it expects to do a great deal toward placing young people in the industry.

There is also the challenging opportunity to see that those now in the industry, and those to come, have greater access to published information about mortgage lending—a field which has been neglected so far. The Trust Fund is a charitable trust supported by contributions. It has set its aims high; and with the cooperation of those in the industry it can, and will, do an excellent job for mortgage banking in education and research.

requires management, why have some of the major life companies gone into the development and operation of large-scale housing projects?" Since life companies are restricted to a very small percentage of their total assets which may be legally invested in the purchase of commercial real estate, and because of a rather limited supply of such properties with satisfactory leases and tenants, these companies have had to find other outlets for the investment of their funds. Life companies owned residential housing, as of December 31, 1954, in the aggregate amount of \$456,000,000. While these housing projects, which served a public need, supplied an outlet for some of their funds, they nevertheless have placed these companies in a "going business."

SALE AND LEASE-BACKS

(Continued from page 29)

is as good or better than the usual mortgage loan. My answer is that I do not know, nor have I heard, of a single instance where a life company or other institutional purchaser of commercial properties, so leased, have suffered any loss during the past thirteen years through the default of a lessee in the payment of rentals. Considering that substantially more than \$1,250 million have been placed in this type of investment during this period, does this not, at least in a good measure, answer this question?

But someone may ask, "Is the experience of the past thirteen years a sufficiently accurate barometer in determining the merits of these investments, in view of the favorable conditions which business has enjoyed during these years?" One thing is certain, namely, that these investments will be more secure than the preferred stock of the respective corporations which, as lessees, entered into such leases, since rentals are payable before dividends to stockholders.

One of the principal reasons for the purchase by institutional investors of properties subject to an absolute net

lease with companies of acceptable financial standing was to avoid the cares and responsibilities of management. It may then be asked, "Since the ownership of residential housing

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ESCROWS AND MORTGAGES

By **McCUNE GILL**

President, Title Insurance Corp., St. Louis

IT MUST be quite distressing for a mortgage banker to go to all of the trouble necessary to obtain an application for a loan, have an appraisal made and get the loan approved by a lending institution or some governmental department and then to find that the loan cannot be made because of the condition of the title.



McCune Gill

Happily, many of these title difficulties can be solved by an escrow and then the loan can be made. Consider some specific instances where escrows have been found to be the answer to title questions for mortgage bankers:

You are approached by a man who wants to buy a home and wants you to make a mortgage loan to raise part of the purchase price. But the house is owned by three heirs of the deceased former owner and administration on the estate is pending. There probably will be enough cash to pay all claims and taxes against the estate. But such claims and taxes are a lien superior to the lien of your mortgage and your investor will take only a first lien mortgage. This looks like an impossible situation but it isn't. In fact, the solution is quite simple. Have the purchaser put into escrow with a title insurance company his equity money and the proceeds of your loan. The title company will then give your investor a title policy insuring that your mortgage is a first lien. The heirs will execute a deed to the purchaser and he can take immediate possession. You will record your mortgage. The heirs will not get their money until all

claims and taxes against the estate are paid and the administration proceedings are finally settled. If they want some interest on the deposit it can be invested in negotiable government bonds. So your mortgage loan is saved and made possible although at first it seemed to be impossible.

Sometimes there is a prior mortgage that is not yet due and the holder will not accept payment until the due date. Or the prior mortgage secures several notes or bonds and some of them cannot be found immediately. Upon depositing the amount of the unpaid prior mortgage note or notes and interest to maturity with a title company in escrow, it will issue its policy insuring that your mortgage is a first lien. In this way your loan is saved.

The possibility of mechanics' liens being filed within a certain period after the completion of the building presents another problem to the mort-

INTERIM FINANCING

(from page 45)

to widely scattered areas for construction has developed only in the past few years. Many of our members use not one, but many banks, to furnish their construction loan requirements. This type of operation requires a well-organized payout procedure by the mortgage banker, but it also enables him to increase his money supply and often at attractive interest rates.

In any studious analysis, it will become evident that construction lending is an important function of the mortgage banker; and this report is made in an effort to provide suggestions which may help our membership do this job better, safer and more profitably.

gage banker. A title insurance company will check the construction bills and if any are not paid will receive in escrow enough money to pay them and will then issue its mortgagee's title policy free from the possibility of liens by contractors, material men or laborers. In this way your mortgage deal is saved.

Frequently a purchase and mortgage transaction is so complicated that the only way it can be closed is in escrow. This occurs when several properties owned by different persons must be acquired or when one property is owned by several persons or when there are numerous mortgages, judgments, taxes or other liens that must be paid and satisfied. This can only be accomplished by a deposit of the proceeds of the new mortgage, with the amount of equity money necessary to accomplish the purchase and to pay all prior encumbrances, in escrow. In this way the acquisition of the property and the payment of prior liens can be accomplished gradually and the deal finally consummated whereupon your mortgage will become a first lien.

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Detroit MBA Names Officers



Newly-elected officers of the Detroit MBA meet with the 1956 board of governors just before the annual banquet of the organization. Prof. Raymond Rogers, of New York University, was the banquet speaker. From left, seated, are: R. George Ransford, vice president; William J. Stepek, president; Homer B. Wells, secretary treasurer. Ransford is president of the Gleaner Life Insurance Co.; Stepek is vice president of the Detroit Wabek Bank & Trust Co.; and Wells is vice president of Homer Warren & Co. and president of the Detroit Building Owners and Managers Association. Standing are Herman Kersten, Robert J. Hutton, Robert W. Hubert, Stuart Micklethwaite, J. A. Snyder, John W. Matson and Harold N. Finney.

Everett C. Spelman Heads Denver MBA

Everett C. Spelman, vice president, Western Securities Company, Denver, has been elected president of the Denver MBA. Armand Asborne, vice president Central Bank and Trust Company, has been elected vice president and Orlin E. Wood, assistant secretary, Service Investment Company, secretary-treasurer.



E. C. Spelman

OBITUARY: With sorrow we record the death of Stanley H. Trezevant, Sr., a former member of the MBA board of governors, in Memphis. He was founder and president of Stanley H. Trezevant & Company and prior to that was a partner of E. H. Crump in the mortgage and insurance business. He served in the Tennessee legislature in 1913-14 and saw service in World War I. Over

a long period of years he made an important contribution to the work of MBA.

New Members in MBA

ALABAMA, Mobile: E. S. Watts & Co., Inc., Frank Copeland.

CALIFORNIA, Los Angeles: R. A. Rowan & Co., C. A. Saint, president; **Oakland:** North American Title Insurance Company, Marchie Schwartz, executive vice president; **Sacramento:** McClatchy Realty Co., Butler Jack, Jr., secretary-treasurer; **San Francisco:** Northern California Mortgage Company; D. Clair Sutherland.

FLORIDA, Fort Lauderdale: Stockton, Whatley, Davin & Company, S. Ralph Fetter, Jr., assistant vice president; **Pensacola:** Joyner-Heard Company, Leslie C. McLean, vice president.

GEORGIA, Atlanta: Colonial Investment and Mortgage Company, Jack M. Martin, president; Arthur B. L. Martin.

INDIANA, Indianapolis: Hoosier Farm Bureau Life Insurance Co., H. D. Campbell, treasurer.

LOUISIANA, Baton Rouge: Delta Fire and Casualty Company, David W. Thomas, president.

MISSISSIPPI, Jackson: Mississippi Valley Title Insurance Company, O. B. Taylor, Jr., president.

MISSOURI, Clayton: Mortgage Syndicate, Inc., L. L. Serman, president.

NEVADA, Las Vegas: Palomar Mortgage Company, Robert Shaw, vice president.

NEW YORK, New York: Chemical Corn Exchange Bank, Russell L. Hauer, assistant vice president; Stalford & Company, Inc., A. D. Stalford, executive vice president; Union Square Savings Bank, R. H. Brownell, president.

OHIO, Bowling Green: The Bowling Green Banking Co., LeRoy Monroe, president.

PENNSYLVANIA, Bryn Mawr: The Title Insurance Corporation of Pennsylvania, Gordon M. Burlingame, president.

SOUTH CAROLINA, Columbia: McLain and Sherrill, Henry F. Sherrill, partner.

TEXAS, Houston: The National Bank of Commerce of Houston, John E. Whitmore, vice president.

PERSONNEL

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Mortgage loan opportunity with Cincinnati regional office of major insurance company. Age approximately 30-40. Some experience in commercial and industrial loans. Reply in confidence. Write Box 360.

Young man desires position with insurance company in mortgage loan department, eight years experience with major insurance company. Completely familiar with FHA, GI, conventional accounting and collections, real estate and PLB accounting, mortgage schedules of annual statement. Available soon. Write Box 361.

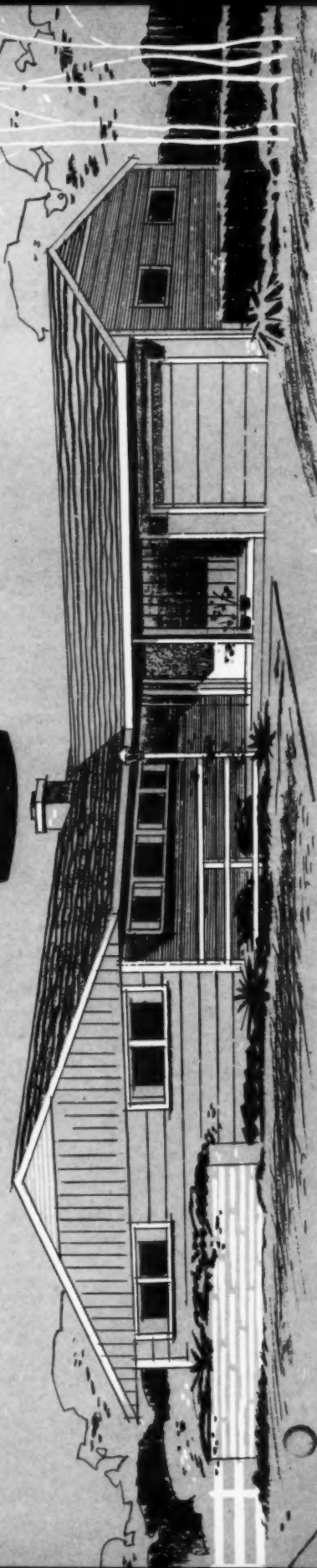
Colorado bank wants experienced mortgage loan man for senior position as department head. Salary and bonus. Write full details including phone number. Box 362.

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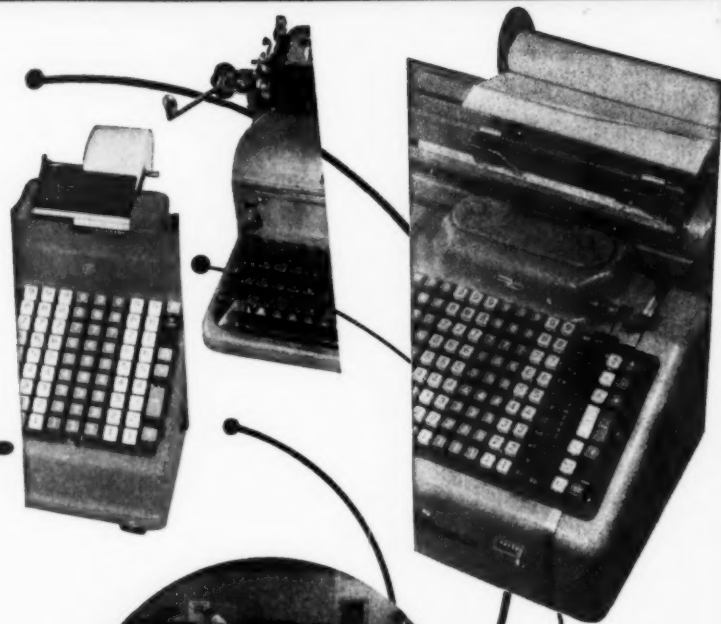
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